

TRANSCRIPT OF RECORD

Supreme Court of the United States

OCTOBER TERM, ~~1940~~ 1941

No. ~~812~~ 34

TEXTILE MILLS SECURITIES CORPORATION,
PETITIONER,

vs.

COMMISSIONER OF INTERNAL REVENUE

WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT
OF APPEALS FOR THE THIRD CIRCUIT

PETITION FOR CERTIORARI FILED MARCH 5, 1941.

CERTIORARI GRANTED MARCH 31, 1941.

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1940

No. 812

TEXTILE MILLS SECURITIES CORPORATION,
PETITIONER,

vs.

COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT
OF APPEALS FOR THE THIRD CIRCUIT

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[fol. 1]

BEFORE UNITED STATES BOARD OF TAX APPEALS

Docket No. 75423

TEXTILE MILLS SECURITIES CORP., Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Appearances:

For Taxpayer: Edmund S. Kochersperger, Esq.

For Comm'r: J. H. Pigg, Esq., R. P. Hertzog, Esq.

DOCKET ENTRIES

1934

Apr. 5—Petition received and filed. Taxpayer notified.
(Fee paid)

Apr. 5—Copy of petition served on General Counsel.

May 25—Answer filed by General Counsel.

June 2—Copy of Answer served on taxpayer.

Aug. 29—Motion for circuit hearing at New York City filed
by taxpayer. 8-31-34 granted to circuit calendar.

1936

Mar. 5—Hearing set May 21, 1936 at New York City.

[fol. 2] May 11—Motion for continuance to next circuit
calendar in New York filed by taxpayer.

May 12—Order of continuance to May 26, 1936, on the
present New York calendar, and be called on the last
mentioned day, in accordance with the notice of hear-
ing heretofore issued, entered.

May 25—Hearing had before Mr. Morris on petitioner's
motion to continue. Continued to Fall Calendar at
Washington, D. C.

May 25—Order continuing to Fall Calendar for hearing in
Washington, D. C. entered.

Oct. 9—Hearing set Dec. 15, 1936.

Dec. 15—Hearing had before Mr. B. B. Turner, Div. 8.
Submitted on the merits. Stipulation of facts filed.
Petitioner's brief due Jan. 29, 1937—Respondent's
brief due March 1, 1937—Petitioner's reply due
March 16, 1937.

1937

Jan. 5—Transcript of hearing of Dec. 15, 1936 filed.

Jan. 29—Brief filed by taxpayer. 1-29-37 copy served.

1938

Sept. 28—Findings of fact and opinion rendered, Mr. Turner, Div. 8. Decision will be entered under Rule 50.

Nov. 8—Computation as to deficiency filed by General Counsel.

Nov. 12—Hearing set Nov. 30, 1938 on settlement.

[fol. 3] Nov. 21—Consent to settlement filed by taxpayer.

Nov. 28—Decision entered, Bolon B. Turner, Div. 8.

1939

Feb. 13—Petition for review by U. S. Circuit Court of Appeals (3) with assignments of error filed by General Counsel.

Feb. 18—Proof of service filed by General Counsel. (Attorney)

Feb. 23—Proof of service filed by General Counsel. (Taxpayer)

Mar. 27—Certified copy of order from the 3rd Circuit re transmission of physical exhibits filed.

Apr. 12—Agreed praecipe filed by General Counsel. Proof of service thereon.

[fol. 4] BEFORE UNITED STATES BOARD OF TAX APPEALS

PETITION—Filed April 5, 1934

First:

Petitioner is a corporation organized under the laws of the State of Delaware and having its place of business in Passaic, New Jersey. Return for the calendar year 1931 was duly filed with the Collector of Internal Revenue at Newark, New Jersey. Returns for the calendar years 1928, 1929 and 1930 were duly filed with the Collector of Internal Revenue at New York City.

Second:

The notice of deficiency (a copy of which is attached and marked Exhibit "A") was mailed to the petitioner on or after February 8, 1934.

Third:

The taxes in controversy are income taxes for the calendar year 1931 and for \$14,085.27 asserted as a deficiency.

Fourth:

The determination of tax and deficiency set forth in the said notice of deficiency is based upon the following errors:

(a) Determination of net income for 1931 instead of a net loss.

(b) Determination of net income for 1930 instead of a net loss, deductible against any 1931 net income.

[fol. 5] (c) Determination of net income for 1929 instead of a net loss, deductible against any 1931 net income.

(d) Failure to apply a regular, consistent theory in the auditing of the petitioner's returns for the years 1928, 1929, 1930 and 1931.

(e) Failure to apply as a credit under the obligatory provisions of the statute, within the period of limitations, the petitioner's overpayment of taxes for the year 1928 or to advise the petitioner of such overpayment in order to permit the due filing of a claim for refund by the petitioner for the year 1928 as a credit against any taxes properly due for the year 1931.

(f) Disallowance of expenses for the years 1929 and 1930 on the ground that such expenses were accrued-expenses for the year 1928, without at the same time transferring as accrued-income for the year 1928, certain items of income reported by the petitioner as income for the years 1929, 1930 and 1931, such transfer to 1928 resulting in a net loss sustained by the petitioner for the year 1931.

(g) Failure to determine net losses for the years 1929 and 1930 as deductions against any net income for the year 1931.

(h) A reversal of position by the respondent to his advantage and to the detriment of the petitioner under circumstances whereby the respondent is now estopped to determine any deficiency for the year 1931.

(i) Erroneous application of Regulations 74, Article 262, [fol. 6] relied upon by respondent in said Exhibit "A".

Fifth:

The petitioner pleads specially that the respondent is now estopped from asserting any deficiency against the petitioner for the year 1931, by the respondent's conduct in the following respects:

Under its system of accounting, as to which the respondent was advised and informed through successive audits over a period of years, the petitioner reported net income for the year 1928 and paid taxes thereon in the amount of \$10,788.67. Said return for the year 1928 was audited by the respondent and approved. For the years 1929 and 1930 the petitioner filed its returns and reported its accounts upon the same system of accounting; the respondent's audits of net losses for the years 1929 and 1930 approved the returns as filed for said years, said approval being made within a period of time whereby if the respondent had then taken his present position there would have been an overpayment of taxes by the petitioner for the year 1928 to be automatically applied by the respondent as a credit against any taxes due for the year 1931 or the petitioner would have been so advised of such overpayment as to permit the filing of a claim for refund as to taxes so paid for the year 1928. Long after the period has expired for the respondent's application by way of credit to 1931 for any overpayment as to 1928, the respondent now attempts to reverse his previous approval of the returns for 1929 and 1930, to his benefit and to the detriment of the petitioner. Having so benefited by his error or misconduct and having induced the petitioner to believe that [fol. 7] its returns for the years 1929 and 1930 correctly reported losses and that the expenses of those years should not be accrued to the year 1928 with resulting overpayment of taxes for the year 1928 and, by such belief, having caused the petitioner to refrain from the filing of a claim for refund in order that such overpayment for the year 1928 might be credited after the expiration of the statute of limitations to and against any lawful taxes assertible for the year 1931, the respondent is now estopped from asserting any deficiency for the year 1931, by the same token that the petitioner would be barred by estoppel if the circumstances were reversed of recovery for an overpayment. By force of such estoppel this honorable Board should enter its order of Judgment for the Petitioner.

Sixth:

The facts upon which the petitioner relies as the basis of this proceeding in addition to the facts heretofore alleged and as an alternative to said pleading by way of estoppel, are as follows:

(a) The alleged deficiency for the year 1931 results from the respondent's disallowance of net losses for the years 1929 and 1930, without changing the reported income for 1931.

(b) The respondent's disallowance of net losses for the years 1929 and 1930 is expressed in said Exhibit "A" as for the following reasons:

"Your contention for the allowance of deductions for expenses incident to the enactment of legislation authorizing the return of property of certain German citizens and corporations seized during the World War, has not been conceded for the reason that the services were performed during the year 1928 when the Settlement of War Claims Act was passed.

"Inasmuch as your books were kept on the accrual basis, the amount of \$143,500.00 so expended should have been accrued as at December 31, 1928."

(c) In its return for the year 1931 the petitioner reported within its Gross Income the item of "Commissions Receivable \$183,048.15".

(d) Said item of \$183,048.15 was audited by the respondent and was found to reflect the collection from "certain German citizens and corporations" of amounts owing by reason of the enactment of said Settlement of War Claims Act in 1928.

(e) The respondent's audit of the petitioner's return for the year 1931 made no change or correction other than a disallowance of the alleged net losses for the years 1929 and 1930.

(f) The net losses for 1929 and 1930 so claimed by the petitioner as deduction for 1931 were \$124,992.39.

(g) The exclusion from gross income of 1931 of said item of \$183,048.15 and the exclusion as deduction of said item of \$124,992.39 would cause the petitioner to have sustained

a net loss in the year 1931 of \$65,670.91 in which event there is no deficiency for 1931.

(h) The net loss reported upon the petitioner's re-[fol. 9] turn for 1931 in the amount of \$7,615.15 has been converted by the respondent into net income for 1931 of \$117,377.24 solely by the exclusion as a deduction of the amount of \$124,992.39 as prior year net losses and the deficiency now asserted for the year 1931 in the amount of \$14,085.27 solely results from the application of the tax rate at 12% to said amount of \$117,377.24.

(i) The contracts by which the petitioner gained the right to commissions for services performed, required that the petitioner bear all expenses connected with the engagement of others in the performance of such services out of such commissions so to be enjoyed.

(k) If the petitioner's expenses became accruals in 1928 then necessarily the petitioner's commissions for services became accruals in 1928 and, in that event, said amount of \$183,048.15 erroneously was reported by the petitioner as income for the year 1931.

(l) The items of \$96,000 for 1929 and \$47,500 for 1930, comprising the total of \$143,500 disallowed as deductions in computing the disallowed net losses in the aggregate of \$124,992.39 and resulting in the deficiency now alleged by respondent for 1931 as shown in said Exhibit "A", became accrued expense of the petitioner in the respective years of 1929 and 1930, for the reason that at no time prior thereto did any of the individuals to whose favor said respective credits were made, have any right to demand said specific [fol. 10] amounts as were respectively agreed upon as then the subject of such demand in said respective years.

(m) In recognition of such creation of right to demand in said respective years, the petitioner made certain actual payments within said years in application in part against said accruals but made no claim of deduction upon its respective returns for said years with respect to such actual payments, because the accruals were inclusive in amount as to said payments.

(n) By force of the nature of the contracts whereunder the petitioner became entitled to commissions for services performed in 1928 and years prior thereto it was impossible for the petitioner to determine the ultimate realization from

those contracts, within the year 1928. For the same reason it was impossible for the petitioner to determine the amounts in 1928 to which any persons would be entitled as compensation for their services performed in 1928 and years prior thereto. Accordingly, it was understood that such compensation would depend upon such realizations from commissions or the expectancy of commissions as various disputes became the subject of apparent adjustment. That situation resulted in the petitioner actually coming to agreements with various persons in the years 1929 and 1930 respectively as to the amount so accrued as expenses in those years and from such agreements resulted the first right of demand accruing to such persons. Partial payments were made within those years respectively and debited to such accruals which at no time prior to such [fol. 11] agreements in the respective years 1929 and 1930 were either ascertainable or determinable as expenses.

(c) If the respondent had taken his present, peculiar position that commissions were accruable when received but the expenses connected with those commissions were accruable in 1928, then the respondent's audits for the years 1928, 1929, and 1930 would have resulted in determinable losses for each of those years (by force of other losses and expenses not connected with the contracts in question) and would have resulted in the respondent's own determination of overpayment of the entire taxes paid for the year 1928, with resulting refund to petitioner.

(p) The respondent now seeks a double collection of taxes from the petitioner through an inconsistent treatment of the accounts of the petitioner, to the monetary advantage of the respondent and corresponding disadvantage to the petitioner who relied upon the prior action of the respondent in approving the net losses for 1929 and 1930 and the petitioner's system of accounting.

(q) The respondent is estopped from making such assertion of deficiency for the year 1931, for the several reasons aforesaid.

(r) The respondent's alleged notice of deficiency for the year 1931 evidenced by Exhibit "A", represents an attempt to assert taxes for prior years which now are barred by the running of the Statute of Limitations and is without any [fol. 12] authority under the law, all due to a reversal of

position as to the correct system of accounting. In no other way may a position of consistency be credited to the respondent. If the petitioner's expenses of 1929 and 1930 should be accrued deductions to 1928, then our 1931 commissions also should have been accrued to 1928 which year is now barred.

Wherefore, the petitioner respectfully prays that this honorable Board may hear its appeal and redetermine the deficiency if any and find the facts as alleged by the petitioner, or determine no deficiency for the reason that the respondent is estopped from asserting any deficiency, and that the Board order such other relief to the petitioner as may be properly due in the premises.

(S.) Edmund S. Kochersperger, Counsel for the
Petitioner, 806 Investment Bldg., Washington,
D. C.

Duly sworn to by Otto E. Kuhn. Jurat omitted in printing.

[fol. 13]

EXHIBIT "A" TO PETITION

IT:AR:B-4.

LHB:6OD.

Feb-8 1934.

Textile Mills Securities Corporation, 84-182 Dayton Avenue, Passaic, New Jersey.

SIRS:

You are advised that the determination of your income tax liability for the year 1931, discloses a deficiency of \$14,085 27 as shown in the statement attached.

In accordance with section 272 of the Revenue Act of 1928 notice is hereby given of the deficiency mentioned. Within sixty days (not counting Sunday as the sixtieth day) from the date of the mailing of this letter, you may petition the United States Board of Tax Appeals for a redetermination of the deficiency.

However, if You Do Not Desire to Petition, you are requested to execute the enclosed form and forward it to the Commissioner of Internal Revenue, Washington, D. C., for the attention of IT:C:P-7. The signing of this form will expedite the closing of your return by permitting an early [fol. 14] assessment of any deficiency and preventing the accumulation of interest charges, since the interest period

terminates thirty days after filing the form, or on the date assessment is made, whichever is earlier: Whereas if This Form is Not Filed, interest at the rate of 6% per annum will accumulate.

Respectfully, Guy T. Helvering, Commissioner, by
(Signed) Chas. T. Russell, Deputy Commissioner.

Enclosures:

Statement.
Form 870.

—
eet-3

(Page 2)

Statement

IT:AR:B-4.
LHB:60D.

In re: Textile Mills Securities Corporation, 84-182 Dayton
Avenue, Passaic, New Jersey

Income Tax Liability

Year	Income Tax Liability	Income Tax Assessed	Deficiency
1931	\$14,085.27	None	\$14,085.27

The deficiency shown herein is based upon facts and data now before the Income Tax Unit in connection with the report dated February 28, 1933, prepared by Revenue Agent [fol. 15] A. J. Auerbach, copy of which you have received.

Careful consideration has been accorded your protests dated April 3, 1933 and December 19, 1933, in connection with the findings of the examining officer and the information submitted at a conference held in this office.

As a result of these findings, your income tax liability has been redetermined as follows:

Net loss reported	(\$7,615.15)
Less:	
Prior year net losses disallowed	124,992.39
Net income corrected	<u>\$117,377.24</u>

Explanation of Adjustments

Net loss reported for 1929	(\$101,405.56)
Less:	
Nontaxable income	6,532.08
Statutory net loss carried forward	(\$94,873.48)

(Page 2)

Textile Mills Securities Corporation		Statement
Brought forward		(\$94,873.48)
Less:		
Expenses incident to legislative work		96,000.00
Net income as corrected for 1929		\$1,126.52
Net loss reported for 1930		(\$134,797.93)
Less:		
Nontaxable income	\$9,805.54	
1929 net loss disallowed	94,873.48	
[fol. 16] Expenses incident to legislative work	47,500.00	152,179.02
Net income as corrected for 1930		\$17,381.09

Your contention for the allowance of deductions for expenses incident to the enactment of legislation authorizing the return of property of certain German citizens and corporations seized during the World War, has not been conceded for the reason that the services were performed during the year 1928 when the Settlement of War Claims Act was passed.

Inasmuch as your books were kept on the accrual basis, the amount of \$143,500.00 so expended should have been accrued as at December 31, 1928.

The following amounts paid attorneys have been classified to show amounts paid for services in connection with contracts and for legislative expenses, as shown in your supplemental brief dated June 26, 1933:

1929	Contract Services	Legislative Work	Total
George S. Ward	\$2,867.60		
Thomas R. Creighton Jr.	3,000.00		
Ivy Lee		\$45,000.00	
F. W. Mondell		46,000.00	
M. B. Schreeve	10,200.00		
Honorable W. F. Martin	5,000.00		
C. Ermelbauer	5,767.50		
A. R. Johnson Jr.		5,000.00	\$122,835.10
Total	\$26,835.10	\$96,000.	\$122,835.10

[fol. 17]

(Page 3)

Textile Mills Securities Corporation

Statement

1930	Contract Services	Legislative Work	Total
George S. Ward	\$10,243.90		
Warren F. Martin		\$40,000.00	
J. Reuben Clark		7,500.00	
H. de Haas	2,500.00		\$60,243.90
Total	\$12,743.90	\$47,500.00	\$60,243.90

Inasmuch as the expenses totalling \$26,835.10 and \$12,743.90 were incurred in connection with contracts involving the personal services of the above-mentioned attorneys in securing the return of property to German citizens and companies from the Alien Property Custodian, for the years 1929 and 1930 respectively, these amounts have been allowed as deductions in accordance with section 43 of the Revenue Act of 1928.

The amounts of \$96,000.00 and \$47,500.00 representing sums spent for the promotion of legislation are not deductible from gross income in accordance with article 262 of Regulations 74 promulgated under the Revenue Act of 1928 and section 43 of the same Act.

Computation of Tax

Net income	\$117,377.24
Less:	
Exemption	none
Amount subject to tax at 12%	\$117,377.24
[fol. 18] Correct income tax liability	\$14,085.27
Income tax previously assessed	none
Deficiency	\$14,085.27

eet-3.

[fol. 19] BEFORE UNITED STATES BOARD OF TAX APPEALS

ANSWER—Filed May 25, 1934

The Commissioner of Internal Revenue, by his attorney, Robert H. Jackson, General Counsel, Bureau of Internal

Revenue, for answer to the petition filed by the above-named taxpayer, admits and denies as follows:

First. Admits that the petitioner is a corporation organized under the laws of the State of Delaware and having its place of business in Passaic, New Jersey. For lack of sufficient information to form a belief, denies the remaining allegations of paragraph First of the petition.

Second. Admits that the notice of deficiency (a copy of which is attached to the petition and marked Exhibit A) was mailed to the petitioner on February 8, 1934.

Third. Admits the allegations of paragraph Third of the petition.

Fourth. Denies that the respondent erred as alleged in subparagraphs (a) to (i), inclusive, of paragraph Fourth of the Petition.

Fifth. Denies the allegations of paragraph Fifth of the petition.

Sixth. (a) and (b). Denies the allegations of subparagraphs (a) and (b) of paragraph Sixth of the petition.

[fol. 20] (c) Admits the allegations of subparagraph (c) of paragraph Sixth of the petition.

(d) to (r). Denies the allegations of subparagraphs (d) to (r), inclusive, of paragraph Sixth of the petition.

Seventh. Denies generally and specifically each and every allegation contained in the petition not hereinbefore admitted or denied.

Wherefore, it is prayed that the petition be denied.

(Signed) Robert H. Jackson, General Counsel,
Bureau of Internal Revenue.

Of counsel: Hartford Allen, David R. Shelton, Special Attorneys, Bureau of Internal Revenue.

[fol. 21] BEFORE UNITED STATES BOARD OF TAX APPEALS

TEXTILE MILLS SECURITIES CORPORATION, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Docket No. 75423

Findings of Fact and Opinion—Promulgated September 28,
1938

The petitioner, a domestic corporation, was engaged generally in representing foreign interests respecting their property and business affairs in the United States. Because of its relationship to such foreign interests it was employed as an agent by various aliens whose property had been seized during the World War under the Trading with the Enemy Act, to present their claims to Congress with a view to obtaining, under anticipated Congressional enactments, either a return of their property or compensation therefor. The petitioner was to bear all expenses in connection with its employment and as compensation was to receive a stated percentage of the money or the value of the property it was able to recover. In pursuance of its employment the petitioner incurred certain expenses which had for their objective the enactment by Congress of the Settlement of the War Claims Act of 1928. Held, on the facts that such expenses constituted ordinary and necessary business expenses within the meaning of the statute and therefore are allowable deductions in determining taxable net income.

[fol. 22] E. S. Kochersperger, Esq., for the petitioner.

J. H. Pigg, Esq., for the respondent.

This proceeding involves a deficiency in income tax determined by the respondent in the amount of \$14,085.27 for the year 1931.

All issues raised in the petition have been disposed of by stipulation with the exception of certain expense items incurred by petitioner in the years 1929 and 1930, the disallowance of which by the respondent has reduced the amount of net loss claimed and carried forward by the petitioner to the taxable year. The expenses in question were incurred by the petitioner in its efforts to procure the enactment of legislation which would permit certain aliens to recover

property seized by the United States during the World War under the Trading with the Enemy Act, and the question presented is whether or not the expenses so incurred constitute allowable deductions within the meaning of the statute.

FINDINGS OF FACT

This proceeding was submitted upon a stipulation of facts and the stipulation is adopted as our findings herein. We shall set forth so much of the facts as is considered necessary for discussion of the issues to be determined.

The petitioner was incorporated in 1924 under the laws of the State of Delaware. Its income tax return for the taxable year was filed with the collector of internal revenue at Newark, New Jersey. Its books were kept and its returns for the years here under consideration were made on the accrual basis.

[fol. 23] During the years material to this proceeding the petitioner's business activities included trading in securities, investing in domestic and foreign properties, and acting as agent for foreign and domestic principals. All of petitioner's officers had official or stockholding connections with one or more textile manufacturing corporations.

In 1924, through the personal contact of its officers with certain German textile interests whose properties in the United States had been seized during the World War under the provisions of the Trading with the Enemy Act, the petitioner was employed to represent those interests in the United States with a view to procuring legislation which would permit the ultimate recovery of their properties. The properties involved had an estimated aggregate value of \$60,000,000 and in the event of success the petitioner was to receive as compensation 10 per cent of the amount or value of the property recovered. All costs and expenses incident to the undertaking were to be borne by petitioner. The contract or contracts were to terminate at the close of the second session of the Sixty-ninth Congress unless in the meantime appropriate legislation had been enacted.

In carrying on this campaign to procure the enactment of the desired legislation, the petitioner engaged the services of various persons and organizations, including Ivy Lee, Warren F. Martin, J. Reuben Clark, and F. W. Mondell. The Ivy Lee organization was employed to handle matters of publicity, including the making of arrangements for

speeches, contacting the press, in respect of editorial comments, and news items. Warren F. Martin, a former special assistant to the attorney general and J. Reuben Clark, a former solicitor of the State Department, were employed in connection with the preparation of propaganda concerning international relations, treaty rights, and the historical policy of the United States relative to enemy-owned property in time of war. F. W. Mondell, an attorney and a former member of Congress, was employed in connection with the preparation and making of proposals and suggestions to members of Congress, "the aim of which was to promote the speedy enactment of the desired legislation". Subsequently Mendell appeared as attorney before the Alien Property Custodian and certain courts on behalf of the alien individuals whose claims were in controversy.

A bill for the settlement of war claims was introduced and passed the House of Representatives during the second session of the Sixty-ninth Congress and was favorably reported to the Senate by the Senate Finance Committee, but had not passed that body when Congress adjourned on March 4, 1927.

Thereafter and prior to the opening of the first session of the Seventieth Congress on December 5, 1927, the petitioner undertook to negotiate new contracts similar in terms to those which had expired. Its efforts resulted in the procuring of new contracts from many of its former principals, but on terms less favorable than in the original contracts. The new contracts provided for the payment of 3 per cent of the amount or value of property received by the claimant and for an additional 2 per cent in respect of money or property paid over to the claimant within one year after enactment of the desired legislation. The new contracts also, as previously, required that the petitioner pay all costs and expenses incurred in its performance thereof. The new agreements were to run for a period of three years beginning with January 1, 1928.

Under the original contracts petitioner had incurred considerable expenses in the form of fees and compensation. In several instances definite arrangements or agreements had not been made with the individuals employed as to the amounts of fees or compensation to be paid for their respective services.

Without further arrangement or agreement, Lee, Martin, Clark, and Mondell continued their work after the close of

the second session of the Sixty-ninth Congress on March 4, 1927. The objective of the campaign so carried on by the petitioner was accomplished during the Seventieth Congress by the passage of the "Settlement of the War Claims Act of 1928", subsequent to which no services were rendered to the petitioner by Lee, Martin, and Clark. Mondell continued to render services, however, during the remainder of the year 1928 and thereafter. These services were legal services, including appearances before the Alien Property Custodian and certain courts, as previously described.

After the close of the Sixty-ninth Congress on March 4, 1927, and during the latter part of 1928 petitioner made various payments to Lee, Martin, Clark, and Mondell, pursuant to the informal agreements or understandings above described, none of which payments are in controversy in this proceeding.

[fol. 26] Early in 1929 petitioner received a bill from Ivy Lee for \$50,000 for services rendered in connection with the contracts mentioned. The amount claimed was in addition to the sums already paid. There was some controversy over the amount, but after discussion of the matter Lee was advised that his claim for additional compensation had been recognized and that payment would be made. He was thereupon credited upon the petitioner's books with the sum of \$50,000 and payments in respect of that sum were subsequently made. In its return, however, petitioner claimed as a deduction only \$45,000 of the \$50,000 item just described. In the same year and under circumstances similar to those set forth with respect to the compensation credited to Lee the amount of Mondell was credited with the sum of \$46,000.

In 1930, Warren F. Martin and J. Reuben Clark were credited on petitioner's books with sums of \$40,000 and \$7,500, respectively, as compensation for services rendered in connection with the above contracts and the amounts so credited were taken by the petitioner as deductions on its 1930 return.

In its return for the year 1929 petitioner reported a net loss of \$101,405.56 and for the year 1930 a net loss of \$134,797.93. For 1931, the year before us, the petitioner brought forward from 1929 a net loss in the amount of \$94,873.48 and from 1930, a net loss, as adjusted, in the amount of \$30,118.91, and reported on its return for 1931 a net loss in the amount of \$7,615.15.

In determining the deficiency herein the respondent reduced the net losses shown on the 1929 and 1930 returns by [fol. 27] the disallowance of the deductions claimed by the petitioner in respect of the amounts credited Lee, Mondell, Martin, and Clark, as outlined above. It is now agreed between the parties that the amount credited to Mondell in 1929 was for legal services rendered "in connection with particular claims of petitioner's principal, after the enactment of the 'Settlement of War Claims Act of 1928' " and the deduction of that amount has been conceded by the respondent as proper. The respondent also concedes that the amount credited to Ivy Lee in 1929 and the amounts credited to Martin and Clark in 1930 were properly accrued on the petitioner's books for those years, but does not concede that they were deductible. The deductibility of these items is the only matter left for our determination. In that respect it is stipulated that if the said items do not represent allowable deductions the correct deficiency for the year 1931 is \$10,186.18 but if they do represent allowable deductions there is no deficiency for that year.

OPINION

TURNER: In his notice of deficiency the respondent rested his disallowance of the deductions here in issue on the provisions of article 262 of Regulations 74,¹ which states in part

¹ Art. 262. Donations by corporations.—Corporations are not entitled to deduct from gross income contributions or gifts which individuals may deduct under section 23 (n). Donations made by a corporation for purposes connected with the operation of its business, however, when limited to charitable institutions, hospitals, or educational institutions conducted for the benefit of its employees or their dependents are a proper deduction as ordinary and necessary expenses. Donations which legitimately represent a consideration for a benefit flowing directly to the corporation as an incident of its business are allowable deductions from gross income. For example, a street railway corporation may donate a sum of money to an organization intending to hold a convention in the city in which it operates, with the reasonable expectation that the holding of such convention will augment its income through a greater number of people

that "Sums of money expended for lobbying purposes, the [fol. 28] promotion or defeat of legislation, the exploitation of propaganda, including advertising other than trade advertising, and contributions for campaign expenses, are not deductible from gross income." He makes no claim that the acceptance of employment such as is involved in this proceeding was not within the scope of petitioner's powers or business. Neither does he make any claim that the expenses incurred were not in fact ordinary and necessary in performing the services required of it under its contract. He now rests his claim wholly upon the decision of the United States Circuit Court of Appeals for the Ninth Circuit in *Sunset Scavenger Co. v. Commissioner*, 84 Fed. (2d) 453, which reversed the Board and approved the regulation cited. At the hearing his counsel stated that "the question in one sentence is whether the Board will follow that decision or whether it won't."

The petitioner admits that the expenses in question were incurred for services relating solely to the promotion of legislation, but claims that they were ordinary and necessary to the performance of the services required under its [fol. 29] contracts and were therefore allowable deductions under the statute, section 23 (a) of the Revenue Act of 1928.²

In *Sunset Scavenger Co. v. Commissioner*, supra, the court states that the statute is "ambiguous because it makes no determination of what is or is not an 'ordinary and necessary' expense" and holds that article 262 of Regulations 74, which limits "the sweeping terms of the statute by prohibiting the deduction" of the expenditures made to avert the enactment of legislation unfavorable to the taxpayer is controlling since the statutory provision allowing

using the cars. Sums of money expended for lobbying purposes, the promotion or defeat of legislation, the exploitation of propaganda, including advertising other than trade advertising, and contributions for campaign expenses, are not deductible from gross income.

² Sec. 23. Deductions from Gross Income.

In computing net income there shall be allowed as deductions:

(a) Expenses.—All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business * * *

the deduction of ordinary and necessary expenses has been reenacted without change in all of the revenue acts after the Revenue Act of 1918, under which the regulation in question was first promulgated. The court further states that the Board in *G. T. Wofford*, 15 B. T. A. 1225, and *Los Angeles & Salt Lake Railroad Co.*, 18 B. T. A. 468, as well as in the case there under consideration, took the view that the expenditures must have been for some illegal purpose to place them outside the provisions of the statute. It was [fol. 30] held that such a conclusion was unsound in that it gave no consideration to the effect of the regulation and was equivalent to reading something into the regulation which could not there be found.

The petitioner questions both the application of the decision in *Sunset Scavenger Co. v. Commissioner*, *supra*, to the facts in the instant case and the reasoning of the court as to the purpose and effect of the regulation. As to the latter, it is argued that article 262 is not an interpretation of the term "ordinary and necessary expenses", but has to do with contributions which depend for their allowance as deductions upon an entirely different provision of the statute, and under such circumstances that Congress can not be said to have approved any such limitation or meaning of the term "ordinary and necessary expenses", as the respondent claims and the court has determined. While it is true that the article in question does appear in the Commissioner's regulation following the quotation of that provision of the statute, section 23 (n),³ which deals with the allowance of charitable and other contributions as deductions, it is to be noted that the statute makes no allowance therein for the deduction of contributions or gifts made by a corporation, and the apparent purpose of the article is to show that, [fol. 31] while expenditures made by a corporation may not be deducted as contributions after the manner of an in-

³ Sec. 23. Deductions from Gross Income.

In computing net income there shall be allowed as deductions:

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(n) Charitable and other contributions.—In the case of an individual, contributions or gifts made within the taxable year

dividual taxpayer, such expenditures are proper deductions as "ordinary and necessary expenses" where they are made legitimately and for the purpose of procuring a direct benefit "to the corporation as an incident of its business." In other words, the article clearly and obviously shows that the test of deductibility of expenditures by corporations is to be found in that portion of the statute governing the deductibility of ordinary and necessary expenses rather than in the provision of the statute covering the deductibility of contributions. Accordingly, the argument of petitioner that the Commissioner's regulation has no relation to the provision of the statute providing for the deduction of "ordinary and necessary expenses" must be regarded as unsound.

On the facts a distinction can be drawn between the instant case and *Sunset Scavenger Co. v. Commissioner*, supra, but in our opinion the distinguishing facts do not take the instant case outside the ruling of the court. It is true that in *Sunset Scavenger Co. v. Commissioner* the legislation in respect of which the expenditure was made would have directly affected the business in which the taxpayer was engaged, while in the instant case the petitioner was not promoting or opposing legislation which directly affected the business in which it was regularly engaged, but as an agent, was seeking to promote legislation for the benefit of others and its compensation was to be received for services rendered as such agent and not from the possible effect [fol. 32] the legislation might have on petitioner's business. In other words, the petitioner was lobbying in behalf of legislation for its own benefit only in so far as it would receive compensation for such lobbying activities from the parties who were to be directly affected and benefited. The activities, however, were none the less lobbying activities and the language of the regulation is sufficiently broad to cover the expenditures of both principal and agent. We are, therefore, unable to find the distinction claimed by the petitioner between the instant case and that of the *Sunset Scavenger Co.*

Accordingly, if we conclude, as did the court in *Sunset Scavenger Co. v. Commissioner*, that the regulation is to be applied in all cases where the activities in respect of which the expenditures are made may reasonably be said to fall within the terms of the regulation, we need go no further, even though the expenses are in fact ordinary and necessary

to the conduct of the taxpayer's business. In applying the statute and the regulation, however, the Board has consistently considered the facts in each particular case and has reached its conclusion as to whether or not the expenditures were in fact ordinary and necessary. See particularly *Sunset Scavenger Co.*, 31 B. T. A. 758, and *Los Angeles & Salt Lake Railroad Co.*, supra. With all due respect to the honorable court, we feel that the facts herein are such that obligatory application of the regulation would result in misapplication of the statute in the instant case. Compare *William P. Kyne*, 35 B. T. A. 202, wherein it appears that there was some question as to the legality of the business in [fol. 33] which petitioner was engaged, and *Lelia S. Kirby*, 35 B. T. A. 578, wherein it does not appear that the activities of the Southern Tariff Association, to which the petitioner made contributions, had a direct bearing on petitioner's business.

In section 12 of the Trading with the Enemy Act, under which the property sought to be recovered was seized, it is stated that "after the end of the war any claim of any enemy or of an ally of enemy to any money or other property received and held by the Alien Property Custodian or deposited in the United States Treasury, shall be settled as Congress shall direct." (40 Stat. 424.) Obviously the only recourse for the restitution of the property so seized was with Congress, and in our opinion the language of the statute was in effect an invitation to the parties whose property had been seized to present their claims to Congress at the end of the war. *Cummings v. Deutsche Bank*, 300 U. S. 115, 120, 121. They were aliens and consequently were at some disadvantage in preparing and presenting their claims, and it was logical that they should seek aid and assistance in this country. The petitioner was engaged generally in the representation of foreign interests in connection with their property and business affairs in the United States and it was in keeping with the circumstances of both parties and the relationship between them that the petitioner should be employed by the particular group of aliens referred to herein in their efforts to recover the property which had been seized. The respondent has made no claim, as we have pointed out, that such employment was outside the scope of petitioner's powers or business and we have concluded from [fol. 34] the record that the services rendered were necessary for the accomplishment of the desired result. There

has been no showing that the petitioner indulged in any questionable practices in carrying out the purposes of its employment and no showing or claim that the activities in respect of which the expenses were incurred were against public policy. Cf. *National Outdoor Advertising Bureau, Inc. v. Helvering*, 89 Fed. (2d) 878. Accordingly we are unable to reach any conclusion except that the expenses here in question were in fact "ordinary and necessary" in the conduct of petitioner's business and, having reached that conclusion, it is our opinion that the statute directs their allowance as deductions in determining petitioner's net income. Cf. *Lucas v. Wofford*, 49 Fed. (2d) 1027, affirming 15 B. T. A. 1225.

Reviewed by the Board.

Decision will be entered under Rule 50.

DISSENTING OPINION

BLACK, dissenting:

Article 262 of Treasury Regulations 74, quoted in the majority opinion, provides, among other things, as follows: "Sums of money expended for lobbying purposes, the promotion or defeat of legislation, the exploitation of propaganda, including advertising other than trade advertising, and contributions for campaign expenses, are not deductible from gross income." I think this is a wholesome regulation and correctly interpretative of the law. There seems to be little, if any, doubt that the expenditures which the petitioner sought to deduct as ordinary and necessary business expenses and which the Commissioner has disallowed as deductions from gross income fall within the foregoing regulation. The majority opinion, as I read it, concedes that fact, but holds that the regulation, when applied to expenditures such as were made in the instant case and disallowed by the Commissioner, is too broad and reads something into the law which is not there. I am unable to agree with that interpretation.

The Ninth Circuit in the *Sunset Scavenger Co.* case, cited in the majority opinion, gave unqualified approval to the quoted Treasury regulation as being a reasonable and correct interpretation of the law.

In *William P. Kyne*, 35 B. T. A. 202, and *Lelia S. Kirby*, 35 B. T. A. 578, we cited and followed the court's opinion

in the Sunset Scavenger Co. case. I am not convinced that we should depart from that position in the instant case. It is perfectly true, as the majority opinion points out, that there are some differences in the facts in the Kyne and Kirby cases from the facts of the instant case, but I do not think these differences are sufficient to justify a distinction and a different ruling in the instant case from that which we made in the Kyne and Kirby cases. I, therefore, record my dissent from the majority opinion and think the decision on this point should be for the Commissioner.

Mellott and Disney agree with this dissent. (Seal.)

[fol. 36] BEFORE UNITED STATES BOARD OF TAX APPEALS

DECISION—Entered Nov. 28, 1938

Pursuant to the Findings of Fact and Opinion of the Board promulgated September 28, 1938, the respondent herein having on November 8, 1938, filed a recomputation and the petitioner having on November 21, 1938 filed an acquiescence therein, now therefore, it is

Ordered and Decided: That there is no deficiency or overpayment in income tax for the year 1931.

(S.) Bolon B. Turner, Member. (Seal.)

Entered Nov. 28, 1938.

[fol. 37] IN UNITED STATES CIRCUIT COURT OF APPEALS, THIRD CIRCUIT

PETITION FOR REVIEW AND ASSIGNMENTS OF ERROR—Filed February 13, 1939

Now comes the Commissioner of Internal Revenue, by his attorneys, James W. Morris, Assistant Attorney General, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, and John M. Morawski, Special Attorney, Bureau of Internal Revenue, and respectfully shows:

I

Jurisdiction

The petitioner on review (hereinafter referred to as the Commissioner) is the duly appointed, qualified and acting

Commissioner of Internal Revenue of the United States, holding his office by virtue of the laws of the United States.

The respondent on review, Textile Mills Securities Corporation, (hereinafter referred to as the taxpayer) is a corporation organized under the laws of the State of Delaware and having its place of business in Passaic, New Jersey. The said Textile Mills Securities Corporation filed its income tax return for the calendar year 1931 with the Collector of Internal Revenue for the Fifth District of New Jersey, whose office is located at Newark, New Jersey, and [fol. 38] within the judicial circuit of the United States Circuit Court of Appeals for the Third Circuit.

The Commissioner files this petition pursuant to the provisions of Sections 1001, 1002 and 1003 of the Revenue Act of 1926, as amended by Section 603 of the Revenue Act of 1928, as amended by Section 1101 of the Revenue Act of 1932, as amended by Section 519 of the Revenue Act of 1934.

II

Prior Proceedings

On February 8, 1934, the Commissioner determined a deficiency in income tax against the taxpayer for the year 1931 in the amount of \$14,085.27, and sent by registered mail a notice of said deficiency in accordance with the provisions of Section 272 of the Revenue Act of 1928. Thereafter, and on April 5, 1934, the taxpayer filed an appeal from the said determination with the United States Board of Tax Appeals.

The case was tried before the United States Board of Tax Appeals on December 15, 1936.

On September 28, 1938 the Board of Tax Appeals promulgated its findings of fact and opinion (38 B. T. A.—No. 82) and on November 28, 1938 entered its decision, wherein it was ordered and decided that there is no deficiency or overpayment in income tax for the year 1931.

III

Nature of Controversy

The question presented to the Board of Tax Appeals was [fol. 39] whether taxpayer is entitled to deduct certain expenses which were incurred by it in its effort to procure the

The taxpayer is a domestic corporation organized under the laws of Delaware. The Board of Tax Appeals found that in 1924, through the personal contact of its officers with certain German Textile interests, whose properties in the United States had been seized during the World War under the provisions of the Trading with the Enemy Act, the taxpayer was employed to represent those interests in the United States with a view of procuring legislation which would permit the ultimate recovery of their property, which had an aggregate value of \$60,000,000.00. In the event of success, the taxpayer was to receive as compensation 10 per cent of the amount or value of the property recovered. All costs and expenses incident to the undertaking were to be borne by the taxpayer. The contracts were to terminate at the close of the second session of the Sixty-ninth Congress, unless in the meantime appropriate legislation had been enacted.

In carrying out this campaign to procure the enactment of the desired legislation, the taxpayer engaged the services of various persons and organizations, including Ivy Lee, Warren F. Martin, J. Reuben Clark and F. W. Mondell. The Lee organization was employed to handle matters of publicity, including the making of arrangements for speeches, contacting the press, in respect of editorial comments, and news items. Martin, a former Special Assistant to the Attorney General, and Clark, a former Solicitor of [fol. 40] the State Department, were employed in connection with the preparation of propaganda concerning international relations, treaty rights, and the historical policy of the United States relative to enemy-owned property in time of war. Mondell, an attorney and former Member of Congress, was employed in connection with the preparation and making of proposals and suggestions to Members of Congress, the aim of which was to promote the speedy enactment of the desired legislation. Subsequently Mondell appeared as attorney before the Alien Property Custodian and certain courts on behalf of the alien individuals whose claims were in controversy.

A bill for settlement of war claims failed to pass the Sixty-ninth Congress. However, the taxpayer secured new contracts and continued its efforts, with the result that the Settlement of War Claims Act of 1928 was passed by the Seventieth Congress.

In connection with its campaign for the promotion of

legislation, taxpayer incurred certain expenses which are in controversy, namely, \$50,000.00 credited to Ivy Lee in 1929, and \$40,000.00 and \$7,500.00 credited to Warren F. Martin and J. Reuben Clark, respectively, in 1930. These items were disallowed as deductions by the Commissioner in accordance with Article 262 of Regulations 74 promulgated under the Revenue Act of 1928. The Board, however, held that these expenses were in fact "ordinary and necessary" in the conduct of taxpayer's business and that the statute directs their allowance as deductions in determining taxpayer's net income.

[fol. 41]

IV

Assignments of Error

The Commissioner avers that in the record and proceeding before the Board of Tax Appeals and in the opinion and final decision rendered and entered by the Board of Tax Appeals, manifest error occurred and intervened to the prejudice of the Commissioner who now assigns the following errors and each of them, which he avers occurred in said record, proceeding, opinion and final decision so rendered and entered by the Board of Tax Appeals:

1. The Board of Tax Appeals erred in holding and deciding that there is no deficiency or overpayment in income tax for the year 1931.

2. The Board of Tax Appeals erred in failing to hold and decide that there is a deficiency in income tax for the year 1931 in the amount of \$10,186.18.

3. The Board of Tax Appeals erred in holding and deciding that the amount of \$50,000.00 credited on taxpayer's books to Ivy Lee in 1929 was deductible from gross income for 1929.

4. The Board of Tax Appeals erred in holding and deciding that the amounts of \$40,000.00 and \$7,500.00, credited on taxpayer's books to Warren F. Martin and J. Reuben Clark, respectively, in 1930, were deductible from gross income for 1930.

5. The Board of Tax Appeals erred in holding and deciding [fol. 42] ing that the amounts herein in controversy which taxpayer sought to deduct from gross income do not fall within Article 262 of Regulations 74.

6. The Board of Tax Appeals erred in failing to hold and decide that the amounts herein in controversy which taxpayer sought to deduct from gross income fall within Article 262 of Regulations 74.

5. The Board of Tax Appeals erred in holding and deciding that the facts herein are such that obligatory application of Article 262 of Regulations 74 would result in misapplication of the statute in the instant case.

8. The Board of Tax Appeals erred in holding and deciding that the services rendered in connection with the items in controversy were necessary for the accomplishment of the desired result.

9. The Board of Tax Appeals erred in holding and deciding that the expenses herein in controversy were in fact "ordinary and necessary" in the conduct of taxpayer's business and that the statute directs their allowance as deductions in determining taxpayer's net income.

10. The Board of Tax Appeals erred in that its decision is not supported by the evidence and is contrary to law.

Wherefore, the Commissioner petitions that the decision of the Board of Tax Appeals be reviewed by the United States Circuit Court of Appeals for the Third Circuit, that [fols. 43-44] a transcript of the record be prepared in accordance with law and with the rules of said Court and transmitted to the Clerk of said Court for filing, and that appropriate action be taken to the end that the errors complained of may be reviewed and corrected by said Court.

(Sgd.) James W. Morris, Assistant Attorney General; (Signed) J. P. Wenchel, RLW; (Sgd.) J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue. Of Counsel: John M. Morawski, Special Attorney, Bureau of Internal Revenue.

JMM: spt 2-11-39.

Duly sworn to by John M. Morawski. Jurat omitted in printing.

[fol. 45] IN UNITED STATES CIRCUIT COURT OF APPEALS

NOTICE OF FILING PETITION FOR REVIEW—Filed February 18,
1939

To Edmund S. Kochersperger, Esq., 806 Investment Building, Washington, D. C.:

You are hereby notified that the Commissioner of Internal Revenue did, on the 13th day of February, 1939, file with the Clerk of the United States Board of Tax Appeals, at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Third Circuit, of the decision of the Board heretofore rendered in the above-entitled case. A copy of the petition for review and the assignments of error as filed is hereto attached and served upon you.

Dated this 13th day of February, 1939.

(Signed) J. P. Wenchel, RLW, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue.

Personal service of the above and foregoing notice, together with a copy of the petition for review and assignments of errors mentioned therein, is hereby acknowledged this 15 day of February, 1939.

(Seal) Edmund S. Kochersperger, Attorney for Respondent on Review.

spt 2-11-39.

[fol. 46] IN UNITED STATES CIRCUIT COURT OF APPEALS

NOTICE OF FILING PETITION FOR REVIEW—Filed February 23,
1939

To Textile Mills Securities Corporation, Passaic, New Jersey:

You are hereby notified that the Commissioner of Internal Revenue did, on the 13th day of February, 1939, file with the Clerk of the United States Board of Tax Appeals, at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Third Circuit, of the decision of the Board heretofore rendered in the above-entitled case. A copy of the petition for review and the

assignments of error as filed is hereto attached and served upon you.

Dated this 13th day of February, 1939.

(Signed) J. P. Wenchel, R. L. W., J. P. Wenchel,
Chief Counsel, Bureau of Internal Revenue.

Personal service of the above and foregoing notice, together with a copy of the petition for review and assignments of errors mentioned therein, is hereby acknowledged this 20 day of February, 1939.

(Seal) Textile Mills Securities Corp., O. E. Kuhn,
Asst. Treasurer, Respondent on Review.

sept 2-11-39.

[fol. 47] BEFORE UNITED STATES BOARD OF TAX APPEALS

STIPULATION OF FACTS—Filed December 15, 1936

It is hereby stipulated and agreed by and between the parties hereto, by their respective attorneys, that the following facts may be taken as true, and that the same may be considered by the Board, as offered in evidence by the parties to this proceeding:

1. The petitioner was incorporated under the laws of the State of Delaware during the year 1924. Its income tax return for the calendar year 1931 was made to the Collector of Internal Revenue for the Fifth District of New Jersey, at Newark, New Jersey.

2. Attached hereto and made a part hereof, as Exhibit "A", is a true and correct copy of the notice of deficiency, dated February 8, 1934, from which the petitioner's appeal was taken.

3. The petitioner's books were kept and its income tax returns were filed on the accrual basis.

4. During the years material to this proceeding, the petitioner was engaged in various business activities, including trading in securities, investing in domestic and foreign properties, and acting as agent for foreign and domestic principals. The petitioner's capital stock was held by three individuals who were also its officers, including Charles F. H. Johnson, as its president. All of the petitioner's officers

were likewise officers, directors and/or stockholders of one [fol. 48] or more manufacturing corporations in the textile industry.

5. During the year 1924, as a result of the personal acquaintances existing between petitioner's officers and certain German textile interests whose properties in the United States had been seized during the World War, under the provisions of the Trading with the Enemy Act, 40 Stat. 411, the services of the petitioner were engaged by various German interests, hereinafter referred to as claimants and/or principals, to the end that the petitioner should represent such claimants, as their agent in the United States, with a view to presenting their cause to the Congress of the United States, and the ultimate recovery by the claimants, under anticipated legislative enactments, of their properties, or compensation therefor. The original agreements in respect of such representation by the petitioner were entered into through the Reichsverband der Deutschen Industrie, a German organization similar to the United States Chamber of Commerce, the contracts being between the various claimants and the petitioner. By the time the petitioner embarked upon its program of performance, during the early part of the year 1926, it had entered into such representation contracts with claimants whose seized properties had an estimated aggregate value of \$60,000,000.00. Under these representation contracts, the petitioner's compensation, in the event of success, was ten per cent, (10%) of the amount of value of the property recovered; all costs and expenses incident to the petitioner's undertakings to be borne by petitioner. Each of these original representation contracts contained a limitation clause, whereby all rights of the petitioner to compensation, and otherwise, terminated with the [fol. 49] close of the Second Session of the Sixty-ninth Congress, unless, in the meantime, appropriate legislation had been enacted.

6. The obligations of the petitioner under the aforesaid representation contracts were such as necessitated the conduct by the petitioner of an extensive educational campaign, the object of which was to acquaint and impress upon the American people and their representatives in Congress, the justice of the claims of the petitioner's principals. Such a campaign was conducted by the petitioner at its own expense. The carrying on of this campaign involved the

gathering and dissemination of historical data and precedents in respect of the policy of the United States relative to enemy-owned properties within its borders in times of war, international relations, treaty rights, etc., as well as the preparation and making of appropriate proposals and suggestions to Members of Congress, with a view to the expeditious enactment of the sought-for legislation. For these purposes the petitioner engaged the services of various persons and organizations, including Ivy Lee, W. F. Martin, J. Reuben Clark, and F. W. Mondell. The services of the "Ivy Lee" organization were utilized in connection with matters of publicity; including the making of arrangements for speeches and speakers around the country, cooperating with the Press in editorial comments, as well as news items, and work of a general publicity nature. The services of W. F. Martin and J. Reuben Clark were utilized in connection with the preparation of propaganda concerning international relations, treaty rights, and the historical policy of the United States relative to enemy-owned property in times of war. Their views on these subjects were expressed [fol. 50] in several publications; one, during the year 1926, which was presented to the Senate by a Member of that Body, entitled "American Policy Relative to Alien Enemy Property", which was published as Senate Document No. 181, Sixty-ninth Congress, Second Session, a true and correct copy of which is attached hereto and made a part hereof as Exhibit "B"; another, entitled "Status of Ex-enemy Property, Interpretation of Treaties and Constitution", being a forty-three page pamphlet, which was widely distributed through the facilities of "Ivy Lee", and otherwise, a true and correct copy of which is attached hereto and made a part hereof, as Exhibit "C". The services of F. W. Mondell, a Washington attorney and former Member of Congress, were utilized, prior to the enactment by Congress of the "Settlement of War Claims Act of 1928", to which enactment further reference will be hereinafter made, primarily in connection with the preparation and making of appropriate proposals and suggestions to Members of Congress, the aim of which was to promote the speedy enactment of the desired legislation. Thereafter, the services of Mr. Mondell were utilized by the petitioner by his appearances before the Alien Property Custodian and certain courts on behalf of certain of the petitioner's principals, whose claims were in controversy.

7. As a result of the campaign carried on by the petitioner, as aforesaid, and other efforts in that direction, a Bill for the settlement of war-claims was introduced in and passed by the House of Representatives during the Second Session of the Sixty-ninth Congress which began on December 6, 1926. This Bill was favorably reported by the [fol. 51] Senate Finance Committee to the Senate where debate thereon was completed, but due to a filibuster there was an adjournment of that Session of the Congress, by limitation, on March 4, 1927, without the enactment of this, and other bills.

8. In the performance of the work incident to the near accomplishment of its objective, as described in paragraph (7), supra, the petitioner had incurred considerable expenses in the form of fees and compensation to those whom it had employed in connection with its campaign for the dissemination of propaganda calculated to promote the desired legislation. Substantial sums on account thereof were paid by the petitioner during the years 1926 and 1927, as well as during the year 1928, after the failure of enactment of the aforesaid Bill. The petitioner's arrangements with several of the persons, whose services it had employed, were informal, and had not been reduced to definite agreements as to the amounts of the fees or compensation to be paid for their respective services. As a result of this situation difficulties and misunderstandings subsequently arose, to which further reference will be hereinafter made.

9. The enactment of legislation permitting of the return of or settlement for the seized properties of the erstwhile enemies of the United States not having been accomplished prior to the close of the Sixty-ninth Congress, all rights of the petitioner under its contracts with its German principals terminated. Thereafter, and prior to the opening of the First Session of the Seventieth Congress, on December 5, 1927, the petitioner undertook, through its representatives in Germany and otherwise, to negotiate new contracts, similar in terms to those which had expired. These efforts [fol. 52] were unsuccessful, although the petitioner did succeed in obtaining new contracts from many of its former German principals on terms less favorable to it than formerly. Typical of these new contracts is the following:

“Agreement made between (name of claimant) of the Republic of Germany, whose address is, —, Germany (here-

inafter called the Claimant) and Charles F. H. Johnson, of 200 Fifth Avenue, New York City, United States of America (hereinafter called the Agent).

“That for and in consideration of the premises and of the mutual promises and undertakings of the Claimant and Agent, hereinafter set forth, the Claimant and Agent agree to and with each other as follows:

“1. The Agent agrees to represent the Claimant in the United States of America and take any and all steps, and perform any and all services which he may deem necessary or advisable to protect the interest of the Claimant in moneys and/or securities or properties now held in trust for the Claimant by the Alien Property Custodian, and to bring about the return of the Claimant's property, and the return of all German money and/or securities or other properties or businesses seized by the United States or any of its Departments, representatives or agents; and said Agent agrees to make or cause to be made such appearance, with counsel to be retained by the Agent at his sole cost and expense before any Congressional Committee, or any Department, Court or Official of the Government of the United [fol. 53] States, as will aid in bringing about such return.

“2. The Agent further agrees to meet all costs and expenses incurred in the performance of his agency and not to render or hold the Claimant in any manner responsible therefor provided, however, that the Agent shall have the right to act for and represent others similarly situated.

“3a. The Claimant agrees at such time and place as the Agent shall direct, to pay to the Agent or his representative three per cent (3%) of any money and/or of the then value of any securities or other property received by the Claimant by or for account of the Claimant from said Alien Property Custodian or from any other branch or department of the United States, or any of its public officials.

“3b. In addition, the said agent shall receive two per cent (2%) in value on the amounts actually paid to the Claimant within one year after enactment of such legislation.

“4. This agreement is executed upon the understanding that it supersedes all previous agreements made by the

Claimant in respect to the subject matter hereof, except in the following particulars: It shall not be construed to empower the Agent hereunder to participate in or claim any benefits, unless otherwise agreed, of any litigation or application now pending in Court or before any governmental department for the return of Claimant's property under any law or decision effected previous to April 1st, 1927.

[fol. 54] "5. This agreement shall be in force for a period of three years beginning with the first of January 1928.

"6. It is further mutually agreed that all differences which might arise shall be submitted to an arbitration court consisting of three members, one appointed by the Agent, one by the Claimant, these two choosing the third who shall act as chairman. In the event that the two appointed members cannot agree upon the chairman then such chairman shall be named by the managing member of the Presidential Board of the Reichsverband der Deutschen Industrie. The decision of the Arbitration court shall be final and binding upon the parties hereto.

"Signed, sealed and delivered," etc.

(Note: The contracts were entered into in Germany in the individual name of the president of the petitioner corporation and then were assigned to the petitioner.)

10. Messrs. Lee, Martin, Clark and Mondell continued their respective services, as hereinabove described, to the petitioner until the enactment of the "Settlement of War Claims Act of 1928", on March 10, 1928, 45 Stat. 254, during the First Session of the Seventieth Congress which began on December 5, 1927, although they were cognizant of the circumstances incident to the failure of the enactment of the necessary legislation prior to the close of the Sixty-ninth Congress, and although no new or more definite agreements or understandings were made between them and the petitioner in respect of the amount of compensation they were to receive for their services in the promotion of the [fol. 55] desired legislation. The objective of the educational campaign so carried on by the petitioner was accomplished by the passage of the "Settlement of the War Claims Act of 1928", supra, subsequent to which no services were rendered to the petitioner by Messrs. Lee, Martin and

Clark. Mr. Mondell, however, continued to render services to the petitioner during the remainder of the year 1928, and thereafter. These services were legal services, Mr. Mondell being required to appear and represent various of the petitioner's principals before the Alien Property Custodian and certain courts, in connection with claims which were in controversy.

11. During the period subsequent to the close of the Second Session of the Sixty-ninth Congress, on March 4, 1927, and the latter part of the year 1928, the petitioner had made various payments to Messrs. Lee, Martin, Clark and Mondell pursuant to the informal agreements or understandings hereinabove referred to, none of which payments are in controversy in this proceeding.

12. During the early part of the year 1929, the petitioner received a bill from "Ivy Lee" for \$50,000, for services theretofore rendered in connection with the petitioner's campaign for the promotion of legislation, in addition to the sums already paid on account thereof. The receipt of this bill by the petitioner gave rise to some controversy as to the amount "Ivy Lee" was to receive for the services rendered by his organization but after a discussion of the matter between the petitioner's officers and directors, the petitioner advised "Ivy Lee" that his claim for such additional compensation had been recognized and accepted by it, [fol. 56] and that payment thereof would be made in the future, as the petitioner's financial position permitted. Thereupon, and during the year 1929, there was credited to the account of "Ivy Lee", on the petitioner's books of account, the sum of \$50,000.00. Payments subsequently made on account thereof have been debited to that account, with corresponding credits to petitioner's cash account.

13. Under circumstances similar to those set forth in paragraph (12), supra, the accounts of F. W. Mondell and A. R. Johnson, Jr., on the petitioner's books, were credited with the respective amounts of \$46,000.00 and \$5,000.00, during the year 1929. It is now agreed that the services for which these two amounts were so entered as accrued accounts payable on the petitioner's books, were legal services rendered by Messrs. Mondell and Johnson in connection with particular claims of the petitioner's principals.

after the enactment of the "Settlement of War Claims Act of 1928", as hereinabove set forth.

14. Under circumstances similar to those set forth in paragraph (12), supra, except for the year during which they transpired, the accounts of Warren F. Martin and J. Reuben Clark, on the petitioner's books, were credited with the respective amounts of \$40,000.00 and \$7,500.00, during the year 1930. Subsequent payments made on these accounts were treated by the petitioner on its books of account in like manner as stated in paragraph (12), supra. The parties hereto agree that these two obligations so incurred and accrued on the petitioner's books of account, as well as the amount of \$50,000.00, referred to and described in paragraph (12), supra, represent expenses incurred by the petitioner directly in connection with the campaign carried on by it, as aforesaid, the purpose of which was accomplished by the enactment by Congress of the "Settlement of War Claims Act of 1928", as aforesaid.

15. In its income tax return for the year 1929, the petitioner reported a net loss of \$101,405.56, computed as follows:

Gross income (exclusive of non-taxable dividend income of \$6,532.08)	\$195,967.16
Less:	
Deductions (not in controversy)	\$201,372.72
Other deductions:	
(a) Ivy Lee	45,000.00
(b) F. W. Mondell	46,000.00
(c) A. R. Johnson, Jr.	5,000.00
	<hr/>
Net loss reported on 1929 return	\$101,405.56

(a) This \$45,000.00 item represents the item of like amount disallowed by the respondent as a deduction, as shown by page (2) of the statement which accompanied the notice of deficiency, Exhibit "A". This is also the same item referred to in paragraph (12), supra, which through

error was reported in the petitioner's 1929 return as \$45,000.00, instead of the correct amount, \$50,000.00.

(b) and (c). These amounts of \$46,000.00 and \$5,000.00 represent the items of like amounts disallowed by the respondent as deductions, as shown by page (2) of the statement which accompanied the notice of deficiency, Exhibit "A". They are also the same items as are referred to in paragraph (13), *supra*. The respondent now concedes that [fol. 58] these items, aggregating \$51,000.00, represent allowable deductions for the year 1929.

16. In its income tax return for the year 1930, the petitioner reported a net loss of \$134,797.93, computed as follows:

Gross income (exclusive of non-taxable dividend income of \$9,805.54)				\$203,958.95
Less:				
Deductions (not in controversy)				\$196,383.40
Other deductions:				
(d) Warren F. Martin		40,000.00		
(e) J. Reuben Clark		7,500.00		
Net loss—1929	101,405.56			
Less:				
1929 dividends	6,532.08	94,873.48	338,756.88	
Net loss reported on 1930 return				\$134,797.93

(d) and (e). These amounts of \$40,000.00 and \$7,500.00 represent the items of like amounts disallowed by the respondent as deductions, as shown by page (3) of the statement which accompanied the notice of deficiency, Exhibit "A". These are also the same items of like amounts referred to and described in paragraph (14), *supra*.

17. In its income tax return for the year 1931, the petitioner reported a net loss of \$7,615.15, computed as follows:

[fol. 59]

Gross income (exclusive of non-taxable dividend income of \$9,856.60)				\$260,904.75
Less:				
Deductions (not in controversy)		\$143,527.51		
Other Deductions:				
1929 net loss, as above			94,873.48	
1930 net loss, per return		\$134,797.93		
Less:				
1930 dividends	\$9,805.54			
1929 net loss	94,873.48	104,679.02	30,118.91	268,519.90
Net loss reported on 1931 return				\$7,615.15

18. The petitioner waives the assignments of error contained in subdivisions (d), (e), (f) and (h) of paragraph "Fourth" of its petition. The respondent concedes that if the items remaining in controversy, i. e., \$45,000.00 for the year 1929, and \$40,000.00 and \$7,500.00 for the year 1930, represent allowable deductions, they were properly accrued on the petitioner's books during those years.

19. If the items remaining in controversy, referred to in paragraph (18), supra, do not represent allowable deductions, the correct deficiency for the year 1931 is \$10,186.18. If said items do represent allowable deductions, there is no deficiency for the year 1931.

(Sgd.) Edmund S. Kochersperger, Counsel for Petitioner. (Sgd.) Morrison Shafroth, Chief Counsel, Bureau of Internal Revenue, Counsel for Respondent.

[fol. 60] IN UNITED STATES CIRCUIT COURT OF APPEALS

ORDER RE TRANSMISSION OF EXHIBITS—Filed March 27, 1939

Upon consideration of the petitioner's motion and the causes shown in support thereof, and it appearing to the Court that the respondent has no objection to the entering of the order therein moved,

It is by the Court this 24th day of March, 1939,

Ordered: That the Exhibits "B" and "C", together with three copies thereof, which exhibits are attached to and made a part of the Stipulation of Facts called for by the Praeceptum for Record herein, be transmitted in physical form by the Clerk of the United States Board of Tax Appeals to the Clerk of this Court, to be held in the custody of the Clerk of this Court and not incorporated in the printed transcript of record on review, but to be produced at the hearing of this cause for the benefit of the Court and counsel as part of the record on review; and it is further

Ordered: That the Clerk of this Court transmit forthwith a certified copy of this Order to the Clerk of the United States Board of Tax Appeals, to be by him incorporated in the record on review as transmitted.

By the Court, John Biggs, Jr., Circuit Judge.
JMM spt 3-03-39

Order to Transmit Physical Exhibits Received and Filed
March 24, 1939. Wm. P. Rowland, Clerk.

[fol. 61] Clerk's Certificate to foregoing paper omitted in printing.

[fol. 62] BEFORE UNITED STATES BOARD OF TAX APPEALS

PRAECEPTUM FOR RECORD—Filed April 12, 1939

To the Clerk of the United States Board of Tax Appeals:

You will please prepare, transmit and deliver to the Clerk of the United States Circuit Court of Appeals for the Third Circuit, copies duly certified as correct of the following documents and records in the above-entitled cause in connection with the petition for review by the said Circuit Court of Appeals for the Third Circuit, heretofore filed by the Commissioner of Internal Revenue:

1. Docket entries.
2. Pleadings:
 - (a) Petition.
 - (b) Answer to Petition.

3. Findings of Fact and Opinion promulgated September 28, 1938.

4. Decision entered November 28, 1938.

5. Petition for Review.

6. Notices of Filing Petition for Review.

7. Stipulation of Facts, including Exhibits B and C, but excluding Exhibit A. Said Exhibits B and C, together with three copies thereof, to be transmitted in physical form pursuant to order of Court dated March 24, 1939.

[fol. 63] 8. Court Order dated March 24, 1939.

9. This Praecipe.

(Signed) J. P. Wenchel, R L W, Chief Counsel,
Bureau of Internal Revenue.

Service of a copy of the within Praecipe is hereby admitted this 3rd day of April, 1939.

No objections.

Edmund S. Kochersperger, Attorney for Respondent
on Review.

JMM-vbd-3-28-39.

[fol. 64] Clerk's Certificate to foregoing transcript omitted in printing.

[fol. 65] IN THE UNITED STATES CIRCUIT COURT OF APPEALS
FOR THE THIRD CIRCUIT, OCTOBER TERM, 1939

No. 7056

COMMISSIONER OF INTERNAL REVENUE, Petitioner,

vs.

TEXTILE MILLS SECURITIES CORPORATION, Respondent

And afterwards, to wit, the 4th day of October, 1939, come the parties aforesaid by their counsel aforesaid, and this case being called for argument sur pleadings and briefs, before the Honorable John Biggs, Jr., Honorable Albert B. Maris and Honorable William Clark, Circuit Judges, and the Court not being fully advised in the premises, takes further time for the consideration thereof,

And afterwards, to wit, on the 21st day of May, 1940, enters the following order:

[fol. 66] IN THE UNITED STATES CIRCUIT COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 7056

COMMISSIONER OF INTERNAL REVENUE, Petitioner,

vs.

TEXTILE MILLS SECURITIES CORP., Respondent

Order Directing Re-argument

Before Biggs, Maris and Clark, Circuit Judges

It is hereby Ordered that the above entitled case be restored to the calendar for rehearing, and that the reargument be fixed for Monday, July 1, 1940, before the court en banc.

John Biggs, Jr., Circuit Judge.

Philadelphia, May 21, 1940.

[fol. 67] IN THE UNITED STATES CIRCUIT COURT OF APPEALS
FOR THE THIRD CIRCUIT, OCTOBER TERM, 1939

No. 7056

COMMISSIONER OF INTERNAL REVENUE, Petitioner,

vs.

TEXTILE MILLS SECURITIES CORPORATION, Respondent

And afterwards, to wit, the 1st day of July, 1940 come the parties aforesaid by their counsel aforesaid, and this case being called for re-argument sur pleadings and briefs, before the Honorable John Biggs, Jr., Honorable Albert B. Maris, Honorable William Clark, Hon. Charles Alvin Jones and Hon. Herbert F. Goodrich, Circuit Judges, and the Court not being fully advised in the premises, takes further time for the consideration thereof,

And afterwards, to wit, on the 7th day of December, 1940, come the parties aforesaid by their counsel aforesaid, and the Court, now being fully advised in the premises, renders the following decision:

[fol. 68] IN THE UNITED STATES CIRCUIT COURT OF APPEALS,
FOR THE THIRD CIRCUIT, OCTOBER TERM, 1939

No. 7056

COMMISSIONER OF INTERNAL REVENUE, Petitioner,

v.

TEXTILE MILLS SECURITIES CORPORATION, Respondent

On Petition for Review of Decision of the United States
Board of Tax Appeals

OPINION—Filed December 7, 1940

Before Biggs, Maris, Clark, Jones and Goodrich, Circuit
Judges

BIGGS, Circuit Judge:

Facts

Textile Mills Securities Corporation, the respondent taxpayer, is a Delaware Corporation. Its charter is not in

evidence, but it is stipulated that the taxpayer's business activities included trading in securities, investing in properties and acting as an agent for foreign and domestic principals. It also appears that all of the taxpayer's officers had connections either by way of official position or stock ownership in one or more textile manufacturing corporations. These officers were in touch with German textile corporations whose properties had been seized by the Alien [fol. 69] Property Custodian during the First World War under the provisions of the Trading with the Enemy Act (50 U. S. C. A. Appendix). In 1924 the taxpayer was employed by these German interests to represent them in the United States with the object of presenting their cause to Congress, and the ultimate recovery by the claimants, under anticipated legislative enactments, of their properties or compensation therefor. The properties had an estimated aggregate value of \$60,000,000. Under the terms of the contracts under which the taxpayer was employed, in the event of success, the taxpayer was to receive as compensation ten per centum of the amount or value of the properties recovered. The expenses and costs incident to the undertaking were to be borne by the taxpayer. The obligations created by these contracts of retainer were to cease at the close of the Second Session of the Sixty-Ninth Congress unless the legislation sought had been enacted prior to adjournment.

The taxpayer worked vigorously to procure the desired legislation. It employed various persons and organizations, including the Ivy Lee organization, Warren F. Martin, J. Reuben Clark and F. W. Mondell. The Lee organization took charge of publicity, made arrangements for speeches and kept in touch with the press to the end that there might be editorial comment and news items. We think that it may be assumed with fairness that these news stories and editorials were to be favorable to the proposed legislation. Mr. Martin, who had been a former Special Assistant to the Attorney General, and Mr. Clark, who had been a former solicitor in the State Department, prepared brochures entitled respectively "Status of Ex-Enemy Property, Interpretation of Treaties and Constitution" and "American Policy Relative to Alien Enemy Property". The last is a comprehensive study of the history of the treatment of persons and property in war. Mr. Mondell, who is an attorney and a former member of Congress, was employed

by the taxpayer to make proposals and suggestions to members of Congress to promote the speedy passage of the desired legislation. Mr. Mondell also appeared as counsel in hearings before the Alien Property Custodian and certain tribunals on behalf of the taxpayer's clients.

A bill for the settlement of war claims was introduced into and passed by the House of Representatives during the Second Session of the Sixty-Ninth Congress, but did not pass the Senate prior to adjournment. Before the beginning of the First Session of the Seventieth Congress, the taxpayer negotiated new contracts with its clients substantially similar in terms to those which had terminated except for the fact that these new contracts provided for the payment of 3% of the amount or value of property recovered by the claimant and for an additional 2% of the money or property paid over by the United States within one year after the enactment of favorable legislation. In short, the contingent compensation was reduced from 10% of the recovery to a maximum of 5% of the recovery. The new contracts provided that the taxpayer should pay the costs and expenses incurred by it in the performance of its obligations under the contracts. Messrs. Lee, Martin, Clark and Mondell continued their efforts on behalf of the taxpayer. The Seventieth Congress passed the "Settlement of War Claims Act of 1928", 45 Stat. 254. At this time the services of all the persons named except Mr. Mondell terminated. Mr. Mondell continued to render services during the remainder of the year 1928 and thereafter. His services may be characterized as purely legal and consisted of appearances and arguments before the Alien Property Custodian and certain tribunals.

The taxpayer paid to the four men named various sums for their services and reported a net loss for the year 1929 of \$101,405.56 and a net loss of \$134,797.93 for the year 1930. We are concerned only with the year 1931 for the taxpayer pursuant to statutory authority carried forward to that year its net loss for 1929 and 1930, resulting in a net loss for 1931 of \$7,615.15. The Commissioner refused [fol. 71] to accept the losses claimed, disallowing as deductions the sums paid or credited by the taxpayer to Messrs. Lee, Mondell, Martin and Clark for the services performed by them. The Commissioner now concedes that the amounts credited to Mr. Mondell in 1929 were for services rendered "in connection with particular claims of petitioner's prin-

principal, after the enactment of the 'Settlement of War Claims Act of 1928' ", in other words was compensation for legal services, not for procuring legislation, and therefore were properly deductible. The taxpayer claimed that the sums paid or credited to Messrs. Lee, Martin and Clark were deductible as ordinary and necessary expenses paid or incurred during the taxable year in carrying on a trade or business as provided by Section 23 (a) of the Revenue Act of 1928, c. 852, 45 Stat. 791, and were not prohibited by Article 262 of Treasury Regulations 74 as promulgated under that act. The Commissioner contended to the contrary. The Board held in favor of the taxpayer¹ and the petition at bar followed.

The Law

It should be observed that a contract for allegedly procuring the very legislation here involved was twice passed upon by the Court of Appeals for the District of Columbia in two cases, viz., *Gesellschaft Fur Drahtlose Telegraphie M. B. H. v. Brown*, 78 F. (2d) 410, and *Brown v. Gesellschaft Fur Drahtlose Telegraphie M. B. H.*, 104 F. (2d) 227, certiorari denied 307 U. S. 640, the court having before it a suit brought by an attorney to collect a contingent fee for services rendered by him in part in promoting the remedial legislation. In the first case cited the court held the contract to be void as against public policy, stating, p. 412, that there is " * * * a general condemnation of contracts for the procuring of legislation, especially where the legislation is remedial and provides for the assertion of claims against the government, and the contract is for [fol. 72] a contingent portion of a claim that may be given legal status through success in securing the legislation. Such contracts are illegal as tending to corrupt by improper influence the integrity of our political institutions. It is incumbent, therefore, upon the courts to pronounce void any such contract in which the ultimate or probable tendency would be to corrupt or mislead the judgments of legislators in the performance of their duties", citing *Marshall v. B. & O. R. Co.*, 16 How. 314. While the decision in *Marshall v. Baltimore & Ohio Railroad Company* was based in part upon the concealment of the lobby and the lobbyist, the

¹ 38 B. T. A. 623.

general principles there enunciated are applicable to the case at bar for in our opinion those principles have not been modified by the decision in *Steele v. Drummond*, 275 U. S. 199. In the case last cited the Supreme Court pointed out that *Drummond* was not employed by *Steele* or the railroad company to secure the passage of the desired ordinance, but was himself interested in that very end as an owner of property.

The contracts between the taxpayer and its clients were to procure "favor legislation" as distinguished from "debt legislation". See the cases cited p. 229, note 7 to *Brown v. Gesellschaft Fur Drahtlose Telegraphie M. B. H.*, supra. Compensation for procuring the legislation was upon a contingent basis. In the light of both of these considerations, the contracts were null and void. The services performed by the taxpayer and its agents were rendered without suggestion of corruption and, with the exception hereinafter referred to, were not unethical, but as was stated in *Hazleton v. Sheckells*, 202 U. S. 71, 79, "The objection to them rests in their tendency, not in what was done in the particular case." Such contracts as were here made possess a tendency unduly to influence legislative action and to destroy the integrity of legislative institutions. The function of Congress in passing the War Claims Act was purely legislative. It was enacting a remedial statute and providing a method for the adjudication of claims thus created before another tribunal. A distinction is properly made [fol. 73] between contracts for contingent compensation for the prosecution of a debt or contract claim even though such a debt or claim may require legislation and appropriation, and "favor legislation" which creates a debt or claim. The second is prohibited; the first is permissible provided the interest is disclosed and the methods employed are legitimate.

As found by the Board of Tax Appeals, the Lee organization was employed to handle matters of publicity, "including the making of arrangements for speeches, contacting the press in respect of editorial comments and news items." Obviously these news items and editorial comments did not appear under the stated sponsorship of the taxpayer or its clients. The reader of such news comments and editorials including members of Congress could not have known that they emanated from a source inspired by self-interest. Such

practices tend to poison public opinion and should be condemned. See *Marshall v. B. & O. R. Co.*, supra; *Tool Company v. Norris*, 2 Wall. 45; 6 Williston on Contracts, p. 4879; 17 C. J. Contracts § 213. The services rendered by the Lee organization were in and of themselves not otherwise than contrary to public policy.

The taxpayer expended the sums paid to the three individuals named, and now sought to be deducted, in the execution of a void contract. In our opinion such expenditures cannot be deemed to be ordinary. They are outside the norm of ordinary business conduct. A proper construction of Section 23 (a) requires its words to be given their "popular or received import". See *Deputy v. duPont*, 308 U. S. 488, 493, and *Welch v. Helvering*, 290 U. S. 111. Moreover, even if this were not so, the payment of moneys for carrying out a purpose contrary to public policy is by no means ordinary. The great weight of authority supports this view. See *Burroughs Bldg. Material Co. v. Commissioner*, 47 F. (2d) 178; *Chicago R. I. & P. Ry. Co. v. Commissioner*, 47 F. (2d) 990, certiorari denied, 284 U. S. [fol. 74] 618; *Great Northern Ry. Co. v. Commissioner*, 40 F. (2d) 372, certiorari denied, 282 U. S. 855, and *United States v. Sullivan*, 274 U. S. 259.

Quite apart from the foregoing, however, we cannot perceive how the taxpayer's lobbying expenses under the circumstances of the case at bar can be deemed to be necessary expenses in the light of the principles enunciated by the Supreme Court in its decision in *Kornhauser v. United States*, 276 U. S. 145, and *Deputy v. duPont*, supra, p. 494, for there is nothing contained in the stipulation of facts nor any finding by the Board that the services performed by the taxpayer or its agents were the moving or a contributing cause of the passage of the War Claims Act. We cannot perceive how proximate causation can be established between the efforts of lobbyists and the passage of desired legislation except where the efforts extend to actual corruption of individual members of a legislative body for, if the methods employed by the lobbyist be those of permissible persuasion, the legislative body still exercises its freedom of mind and independence of action. As that is the situation ordinarily to be presumed in the absence of a showing to the contrary, there is then interposed between the lobbyist and the law which he desires enacted an independent legislature. The business of the legislature re-

mains the passage of legislation for the public good. It follows that the payments here sought to be deducted could not proximately have served the taxpayer's business and were, therefore, unnecessary as a matter of law. In a far truer sense they resulted proximately from the business of the United States.² Where the law thus determines the want of necessity for expenditures in the operation of a business, it is neither appropriate nor allowable for the Board of Tax Appeals or the courts to find otherwise in [fol. 75] fact because of asserted special purposes or needs of the particular business.

The conclusion, that money spent for lobbying purposes is not deductible as an ordinary and necessary business expense within the intent of the Revenue Acts, is further confirmed by the implication to be derived from recurrent Treasury Regulations denying to corporations the right to deduct such expenditures as donations for business purposes. Thus, Article 262 of Regulations 74, promulgated under Section 23 (n) of the presently applicable Revenue Act (1928), provides in part, that "Sums of money expended for lobbying purposes, the promotion or defeat of legislation, the exploitation of propaganda, including advertising other than trade advertising, and contributions for campaign expenses, are not deductible from gross income". A similar provision was contained in T. D. 2137, 17 Treasury Decisions, Internal Revenue (1915) (pp. 48, 57-58), later appearing as Article 562 of Regulations 45, promulgated under the Revenue Act of 1918. The same provision has appeared without change in regulations promulgated under the Revenue Acts of 1921, 1924, 1926, 1928, 1932, 1934, 1936 and 1938. See Article 562 of Regulations 62, 65 and 69, Article 262 of Regulations 74 and 77, Article 23 (o)-2 of Regulations 86 and Article 23 (q)-1 of Regulations 94 and 101. It may be argued that Article 262 of Regulations 74 is in excess of the Treasury's power to promulgate interpretive regulations for the more efficient

² In this connection it should be noted that Section 12 of the Trading with the Enemy Act provides in part that "After the end of the war any claim of any enemy or an ally of enemy to any money or other property received and held by the alien property custodian or deposited in the United States Treasury, shall be settled as Congress shall direct; * * *."

administration of the Revenue Acts, in that, this particular regulation, which purports to interpret a statutory provision having to do with charitable contributions made by individuals, applies to corporations. Nevertheless, the regulation conforms in purpose with the congressional intent as restricted by the allowance of deduction for business expenses to such as are ordinary and necessary in law as well as in fact. This may not only be reasonably inferred from the legislative history of the repeated enactments of the particular statutory provision without congressional disapproval or rejection of the regulation but that such was and is the congressional intent has more lately been impliedly confirmed by express statutory enactment.

By Sec. 23 (q) of the Revenue Act of 1936, c. 690, 49 Stat. 1648 (26 U. S. C. A. It. Rev. Acts, pp. 830-831), Congress for the first time permitted corporations to deduct, within prescribed limits, donations for charitable uses if "no substantial part of the activities of * * * [the donee] is carrying on propaganda, or otherwise attempting to influence legislation;" etc.³ If money paid to lobbyists were an ordinary and necessary business expense to a corporation, within the intent and understanding of Congress, then the denial by Sec. 23(q) of the right to deduct a contribution when used by the donee for such inhibited purpose could serve no effective end, for, as a business expense, the expenditure would none the less be deductible under Sec. 23 (a) of the Act of 1936. Furthermore, the allowance of deduction for business expenses under Sec. 23(a) of the Act of 1936 is specified in the very same words used in Sec. 23(a) of the Act of 1928. Consequently, moneys spent for lobbying not being ordinary and necessary business expenses under Sec. 23 (a) of the Revenue Act of 1936, as Sec. 23 (q) clearly implies, such expenditures are likewise not ordinary and necessary business expenses under Sec. 23(a) of the Act of 1928. In expressly denying by Sec. 23 (q) of the Act of 1936 any right to a corporate taxpayer to deduct contributions for lobbying, it was the evident intent of Congress to make sure by positive legislative direction that the privilege there granted to corporations of making deductible contri-

³ Repeated verbatim in Sec. 23 (q) of the Revenue Act of 1938, c. 289, 52 Stat. 447, 26 U. S. C. A. Int. Rev. Acts, p. 1016.

butions for charitable uses should not be laid hold of by a taxpayer to gain a credit against tax liability for expenditures which were not, and never had been, deductible as business expense.

For the reasons stated, we conclude that the sums paid by the taxpayer to the three individuals referred to are not ordinary and necessary expenses paid or incurred in carrying on any trade or business. Accordingly, the Commissioner was right in disallowing the credits claimed for the sums so expended.

The Right of the Court to Sit En Banc

This case was originally heard by three circuit judges but before its decision this court, by special order, directed that it be reheard by the court en banc, consisting of the five circuit judges of the circuit in active service. The case has now been heard and considered by the court en banc. The order for rehearing was entered pursuant to Rules 4 and 5 of this court effective March 1, 1940, which are set out in a footnote.⁴ The authority of a circuit court of

⁴Rule 4 (Constitution of the Court. Quorum) is as follows:

"1. The Court—Judges Who Can Constitute It—Number of Judges to Sit. The court consists of the circuit justice, when in attendance, and of the circuit judges of the circuit who are in active service. District judges and retired circuit judges of the circuit sit in the court when specially designated or assigned as provided by law. Three judges shall sit in the court to hear all matters, except those which the court by special order directs to be heard by the court en banc.

"2. Quorum—Adjournment of Court in Absence of—By Whom Adjourned. Two judges shall constitute a quorum. If a quorum does not attend on any day appointed for holding a session of the court, any judge, who does attend may adjourn the court from time to time, or, in the absence of any judge, the clerk may adjourn the court from day to day.

"3. Quorum—Interlocutory Orders in Absence of. Any judge attending when less than a quorum is present may make all necessary interlocutory orders relating to any matter pending in the court preparatory to the hearing or decision thereof."

appeals thus to provide for sittings to be held by all the [fol. 78] circuit judges has been questioned in the Ninth Circuit.⁵ We therefore, deem it important to consider this question. We begin its consideration with a brief reference to the history of the federal judicial system.

The Judiciary Act of September 24, 1789, 1 Stat. 73, set up three categories of federal courts, the Supreme Court, the circuit courts and the district courts, and these courts continued to exist as thus set up (except as to the circuit courts for the period from February 13, 1801 to July 1, 1802) until the effective date of the Judicial Code, January 1, 1912, when the circuit courts went out of existence. The original scheme was for the Supreme Court to be held by justices ap-

Rule 5 (Assignment of Judges) is as follows:

"1. By Whom Assigned—Disqualification of Assigned Judge—Designation of Substitute. The three judges who are to sit in the court at each daily session shall be designated by the senior circuit judge from time to time with the concurrence of a majority of the circuit judges who are in active service. If a judge so designated is unable to attend or is disqualified to sit in a particular matter the senior circuit judge shall designate an active circuit judge to sit in his stead, or, if no active circuit judge is qualified and able to sit, a retired circuit judge or a district judge of the circuit.

"2. Cases to Be Heard by Judges So Assigned. All matters pending in the court, except further proceedings in appeals and petitions previously heard on the merits and matters directed to be heard by the court en banc, shall be heard and decided by the judges who have thus been assigned to sit in the court at the time of hearing, if practicable.

"3. Exceptions. Further proceedings in appeals and petitions previously heard on the merits, except petitions for rehearing, shall be heard and determined by the judges who heard the original appeal or petition, if practicable, and may be heard at any time when the court is not otherwise in session. Petitions for rehearing shall be disposed of in the manner provided by Rule 35. If a rehearing is granted the reargument shall be heard by the judges who heard the original argument, if practicable, unless it is directed to be heard by the court en banc."

⁵ Lang's Estate v. Commissioner, 97 F. (2d) 867.

pointed to it, the district courts to be held by district judges appointed to them, and the circuit courts to be held by supreme court justices and district judges sitting together. In 1802 provision was made for the definite assignment of the Supreme Court justices to the several judicial circuits. When thus assigned and holding circuit court they became known as circuit justices. (See Sec. 605, Rev. Stats.) The law was that the circuit justice of the circuit and the district judge of the district in which a circuit court was held might hold the court together or either of them might hold it separately.

The burden upon the Supreme Court justices at circuit became too heavy and by the Act of April 10, 1869, c. 22, Sec. 2, 16 Stat. 44, it was enacted "That for each of the nine existing judicial circuits there shall be appointed a circuit judge, who shall reside in his circuit, and shall possess the same power and jurisdiction therein as the justice of the Supreme Court allotted to the circuit." This provision was carried into Sec. 607 of the Revised Statutes. The circuit judges thus appointed soon became primarily responsible for holding the circuit courts, largely relieving the circuit justices of this work.

[fol 79] The business of the circuit courts continued to increase, particularly in the Second Circuit, and by the Act of March 3, 1887, c. 347, 24 Stat. 492, the President was directed to appoint for the Second Circuit "another circuit judge, who shall have the same qualifications and shall have the same power and jurisdiction therein that the present circuit judge, has under existing laws." By the Act of March 3, 1891, c. 517, sec. 1, 26 Stat. 826, the President was directed to appoint "in each circuit an additional circuit judge, who shall have the same qualifications, and shall have the same power and jurisdiction therein that the circuit judges of the United States, within their respective circuits, now have under existing laws." Thus after the passage of this act, which, as we shall see, also created the circuit courts of appeals, there were in each circuit two circuit judges, except in the Second in which there were three.

In the light of this background we turn to the provision of Sections 2 and 3 of the Act of March 3, 1891, c. 517, 26 Stat. 826, 827, which created the circuit court of appeals. These sections were as follows:

"Sec. 2. That there is hereby created in each circuit a circuit court of appeals, which shall consist of three judges,

of whom two shall constitute a quorum, and which shall be a court of record with appellate jurisdiction, as is hereafter limited and established * * *."

"Sec. 3. That the Chief-Justice and the associate justices of the Supreme Court assigned to each circuit, and the circuit judges within each circuit, and the several district judges within each circuit, shall be competent to sit as judges of the circuit court of appeals within their respective circuits in the manner hereinafter provided. In case the Chief-Justice or an associate justice of the Supreme Court should attend at any session of the circuit court of appeals he shall [fol. 80] preside, and the circuit judges in attendance upon the court in the absence of the Chief-Justice or associate justice of the Supreme Court shall preside in the order of the seniority of their respective commissions.

"In case the full court at any time shall not be made up by the attendance of the Chief-Justice or an associate justice of the Supreme Court and circuit judges, one or more district judges within the circuit shall be competent to sit in the court according to such order or provision among the district judges as either by general or particular assignment shall be designated by the court: Provided, That no justice or judge before whom a cause or question may have been tried or heard in a district court, or existing circuit court, shall sit on the trial or hearing of such cause or question in the circuit court of appeals * * *."

It will be seen that no provision was made for the appointment of a new group of judges to serve as judges of the circuit court of appeals which the act created. On the contrary it is clear that the court was intended to be held by three judges drawn from the three existing groups of judges who were by section 3 made "competent to sit as judges of the circuit court of appeals within their respective circuits," namely, the circuit justice of the circuit, the circuit judges of the circuit, and the several district judges within the circuit. By the later provisions of the section it is likewise apparent that the circuit justice and the circuit judges were the groups from which the judges of the new court were primarily to come, since it was only if three judges from these groups could not attend that district judges were to be called on. We stress the significant feature of the arrangement, which was that the court was to be staffed by judges who

were not permanently appointed to it, but who were to be drawn from time to time from existing groups of judges having primary responsibility for holding other courts, namely, the circuit justices for the Supreme Court, the circuit judges [fol. 81] for the circuit courts and the district judges for the district courts.

This situation continued until the passage of the Judicial Code of March 3, 1911, c. 231, 36 Stat. 1087. By Section 117 of the Code (36 Stat. 1131, 28 U. S. C. A. § 212), the provisions of Section 2 of the Act of 1891, *supra*, were codified without material change, as follows:

“Sec. 117. There shall be in each circuit a circuit court of appeals, which shall consist of three judges, of whom two shall constitute a quorum, and which shall be a court of record, with appellate jurisdiction, as hereinafter limited and established.”

The Judicial Code abolished on its effective date, January 1, 1912, the existing circuit courts, thus depriving the circuit judges of the courts for which they had been primarily responsible since 1869. We think the Code contemplated that the circuit judges should thereafter be *ex officio* judges of the circuit court of appeals rather than that they should be merely competent to sit in the court—which was their previous status. Although no express provision to this effect appears in the Code as originally enacted, it seems to us to be fairly inferable from two other provisions of the Code. The first is that Sec. 120 of the Code (36 Stat. 1132, 28 U. S. C. A. § 216), into which the provisions of Section 3 of the Act of 1891, *supra*, were carried eliminated the circuit judges from the classes of judges described as “competent to sit” in the court, while retaining in that category “The Chief Justice and the associate justices of the Supreme Court assigned to each circuit, and the several district judges within each circuit.” The other provision supporting the inference is that although the circuit judges were no longer referred to as “competent to sit”, later provisions of the same section which were also carried forward from Section 3 of the Act of 1891, *supra*, clearly showed that the circuit judges were intended to hold the circuit court of appeals and that the district judges should only be designated [fol. 82] to attend if the court could not be made up by the attendance of the circuit justices and circuit judges.

It must be conceded, however, that the Judicial Code, did leave the relation of the circuit judges to the circuit court of appeals in some doubt.

At the time of the passage of the Judicial Code there were, as appears from Section 118 of the Code (36 Stat. 1131), four circuit judges in the second, seventh and eighth circuits. In view of the fact, as we have seen, that the code in Section 117 carried forward the provision of Section 2 of the Act of 1891 that the circuit court of appeals should consist of three judges, an anomalous situation was created with regard, at least, to the second, seventh and eighth circuits if the Code made the circuit judges *ex officio* judges of the court, since in each of those circuits there were four circuit judges. Since their circuit courts had been abolished, these judges had no court at all except the circuit court of appeals, but they obviously could not all be members of a court of three. A serious question thus was presented as to whether the circuit judges had become *ex officio* judges of the circuit court of appeals, and as to whether the circuit court of appeals in those circuits having more than three circuit judges consisted of all the circuit judges or only three of them, and if the latter, which three.

It was evidently to answer these questions that the Act of January 13, 1912, c. 9, 37 Stat. 52, was passed. This Act amended Section 118 of the Judicial Code, which had gone into force twelve days previously, by adding thereto the express provision that "The circuit judges in each circuit shall be judges of the circuit court of appeals in that circuit, and it shall be the duty of each circuit judge in each circuit to sit as one of the judges of the circuit court of appeals in that circuit from time to time according to law."

When the bill which became the Act of 1912 was under consideration in the Senate, Senator Sutherland who was in charge of the bill stated in debate (47 Cong. Record 2736) : [fol. 83] "It makes no change whatever in the existing law except to make it clear that the circuit judges in the various circuits of the United States shall constitute the circuit court of appeals." The report of the Committee on the Judiciary to the House of Representatives (House Rep. 199, 62d Cong., 2d Sess.) likewise said: "This bill deals with a defect in existing law. It makes it clear that the circuit judges shall constitute the circuit court of appeals." We think this legislative history makes doubly certain what is apparent

from the act, namely, that its effect was to make clear that the circuit judges, who theretofore had been primarily responsible for holding the circuit courts, should thereafter instead constitute the circuit court of appeals. The necessary effect of this provision was that in the case of each circuit having more than three circuit judges the size of the court was increased to equal the number of circuit judges authorized by law.

It may be suggested that the provision of the Act of 1912 that it should be the duty of each circuit judge to sit in the circuit court of appeals "from time to time according to law" indicated that the judges were to rotate in sitting. But the sitting is to be "according to law" and we find no provision in the statutes referring to or regulating the designation or assignment of circuit judges to sit in the court "from time to time". On the other hand Section 126 of the Judicial Code (36 Stat. 1132, 28 U. S. C. A. § 223), regulates the times when the circuit courts of appeals shall sit. It is doubtless to these provisions of law that the Act of 1912 refers, thus making it the duty of the circuit judges to sit in the court at the times which the law fixes for its sessions.

We think it necessarily follows from what has been said that the effect of the passage of the Act of 1912 was to amend by implication Section 117 of the Code, which provided that the court should consist of three judges, so as to provide that in the second, seventh and eighth circuits the court should consist of four judges. The further necessary effect was that thereafter as additional circuit judges were authorized the size of the circuit court of appeals of the particular circuit was thereby increased. Consequently by the Act of June 10, 1930, c. 438, 46 Stat. 538, (28 U. S. C. A. § 213d) the Circuit Court of Appeals for the Third Circuit was increased to four judges and by the Act of June 24, 1936, c. 753, 49 Stat. 1903, (28 U. S. C. A. § 213d-1) to five. It is interesting to note that the Act of 1936 which added the fifth judge in the third circuit, directed the President "to appoint an additional circuit judge of the United States Circuit Court of Appeals for the Third Circuit." This act clearly contemplated an addition to the court as well as to the number of circuit judges in the circuit and confirms the construction of the statute which we have adopted.

Other considerations confirm our conclusion that this court consists of five judges, not three. We have seen that

under the amendatory Act of 1912 all five circuit judges of the circuit are judges of the circuit court of appeals. It has always been the practice of the court for all the circuit judges to join in the adoption of rules of court and in the appointment of the clerk and librarian of the court. Conceding this, it may be suggested that but three judges may sit in the court to hear and decide appeals. The act, however, is not capable of such construction. The language is "There shall be in each circuit a circuit court of appeals, which shall consist of three judges". It is not provided that the court, merely when hearing and deciding appeals, shall consist of three judges.

Furthermore, since the act is completely silent as to the manner in which the circuit judges who are to sit in particular sessions of the court are to be selected (a further persuasive indication that all are entitled to sit) if the court consists of three judges only it would appear that the first three circuit judges who ascended the bench at the opening of the term would constitute the court and as such would have power to make rules and orders of procedure limiting the activities of their fellow judges or excluding them entirely from service in the court. Obviously a construction [fol. 85] of an ambiguous statute which would countenance such an absurd situation, improbable as it is, ought not to be entertained.

A court, as distinguished from the quorum of its members whom it may authorize to act in its name, cannot consist of less than the whole number of its members. The whole cannot be less than the sum of its parts. To hold otherwise is not merely to affirm a plain contradiction in terms, but is also to destroy the authority of the court as a court and to open the way to possible confusion and conflict among its personnel and in its procedure and decisions. For an apt illustration see the conflict in decisions disclosed in *John Hancock Ins. Co. v. Bartels*, 308 U. S. 180. It cannot be presumed that Congress intended any such result when it increased the number of circuit judges above three. What we have said makes clear why we cannot agree with Judge Denman's contrary conclusion in *Lang's Estate v. Commissioner*, 97 F. 2d 867. We conclude that this court has power to provide, as it has done by Rule 4 (1), for sessions of the court en banc, consisting of all the circuit judges of the circuit in active service. The court which heard the reargu-

ment of the present case was accordingly lawfully constituted.

What has been said does not affect in any way the provision of Section 117 of the Judicial Code (36 Stat. 1131, 28 U. S. C. A. § 212), that two judges of this court shall constitute a quorum. Consequently it is entirely competent for the court to provide, as it has done by Rule 4, that three judges shall sit to hear all matters unless otherwise specially ordered and that two judges shall constitute a quorum. It has been the practice for the circuit courts of appeals to sit in groups of three judges. We think the practice is an excellent one which should be followed in all but exceptional cases. Where, however, there is a difference in view among the judges upon a question of fundamental importance, and especially in a case where two of the three judges sitting in a case may have a view contrary to that of the other three [fol. 86] judges of the court, it is advisable that the whole court have the opportunity, if it thinks it necessary, to hear and decide the question. Common sense and sound practice dictate that the five judges of this court should be in a position to decide the principles of law and practice to which the court is to be committed. We think the statute does not stand in the way and that the court has the power under existing statutes to sit en banc.

Conclusion.

A majority of the court having concluded that the decision of the Board of Tax Appeals should be reversed, an order will be entered reversing that decision and remanding the cause with the direction to redetermine the tax in accordance with the view expressed by the majority.

I am authorized to state that Judge Jones concurs in this opinion.

CLARK, Circuit Judge, concurring.

The writer of this opinion concurs in the judgment reversing the decision of the Board of Tax Appeals. He is furthermore satisfied about the right of the Court to sit en banc and with the careful and clearly stated analysis of the facts. He wishes, however, to express a somewhat different legal emphasis from that of his brethren constituting, with him, the majority of the Court.

The task of interpreting the obscurities of the various taxing statutes always holds one's technical attention. It

does not so generally hold one's human interest as well. In the case at bar, however, both parts of the judicial nimbus are involved. The exact practices of the case at bar have received the unanimous condemnation of the courts,¹ of the legal text and periodical writers,² of the political scientists,³ [fol. 87] and finally of the intended victims, as various statutes for the regulation of lobbyists bear witness.⁴ The particular victims were the Senators and Representatives of the United States who expressed their feelings in 1934 in other tax legislation where they denied exemption to organizations, a "substantial part of the activities of which is carry-

¹ *Trist v. Child*, 21 Wall. 441.

² 15 Amer. & Eng. Ency. of Law (2d Ed.) p. 969; Legislation—Control of Lobbying, 45 Harvard Law Review 1241 (note); Public Utilities: Expenditures to Influence Public Opinion, 14 Cornell Law Quarterly 233 (note); Contracts—Illegality—Lobbying, 12 Texas Law Review 85 (note); Lobbying Contracts—Contingent Fees—Public Policy, 14 Boston University Law Review 834 (note).

³ Bryce, *The American Commonwealth*, Vol. 1, p. 555, Vol. 2, pp. 66, 514, 520, 653; Pressure Groups and Propaganda, 179 Annals of the American Academy of Political and Social Science, Odegard, Political Parties and Group Pressures p. 68; Bernays, *Molding Public Opinion* p. 82; McKean, *A State Legislature and Group Pressure*, p. 124; Catlin, *The Role of Propaganda in a Democracy* p. 219; Bernays, *Crystallizing Public Opinion: Herring, Lobbying*, 9 Ency. of the Social Sciences 565; Odegard, *Pressure Politics: Herring, Lobbying in Congress*; Crawford, *Inside Story of Lobbying*; Muller, *Lobbying in Congress* (The Reference Shelf, Vol. 7, No. 3).

⁴ Ga. Code Ann. (Michie, 1926) Pen. Code §§ 325 (1)-(5); Ind. Ann. Stat. (Burns, 1926) §§ 8108-16; Kan. Rev. Stat. Ann. (1923) c. 46, §§ 201-10; Ky. Stat. (Carroll, 1930) §§ 1999a 1-8; Me. Rev. Stat. (1930) c. 2, §§ 43-48; Md. Ann. Code (Bagby, 1924) art. 40 §§ 4-14; Miss. Code Ann. (1930) § 5477-84; Md. Rev. Stat. (1919) § 7154; Neb. Comp. Stat. (1929) §§ 50-302 to 304; N. H. Pub. Laws (1926) c. 4 §§ 28-33; N. Y. Legis. Law (1909) § 66; Ohio Gen. Code (Page 1932) §§ 6256-1 to 8; Okla. Stat. 1931 § 2292 (modified); R. I. Gen. Laws (1923) c. 123, §§ 1776-73; S. D. Comp. Laws (1929) §§ 5092-5100; Wis. Stat. (1929) §§ 346.20-26.

ing on propaganda, or otherwise attempting, to influence legislation", 26 U. S. C. A. § 103 (6).

The reason is plain. If argument was a matter of the critique of pure reason, it might be appraised apart from its source. As most argument depends upon disputed premises the burden of verification depends upon (is proportionate to) the impartiality of the arguer. Furthermore there exists the imponderable of sincerity. If a cause is espoused by a person you know or know of, his sincerity or insincerity is bound to affect the weight you give to his presentation. These considerations are particularly applicable in a democracy which tends increasingly away from Burke's theory of representation and toward the continental theory of a mandat impératif. The thought the writer is attempting to express has been well phrased:

"A different element is infused when the nexus between the propagandist and his principal is hidden, for tribunals have developed a policy adverse to the exertion of secret influences upon public bodies. The question of the legality [fol. 88] of not disclosing the identity of those seeking to influence public action first arose in connection with lobbying contracts. Though without the slightest hint of fraud or dishonesty, many contracts were declared void as against public policy. Secrecy doomed the agreement. The cases demand frank dealing, where public interests are concerned. Secret efforts to touch the minds of the legislators, secrecy concerning the connection between lobbyist and client, these are the evils in the eyes of the tribunals. This same attitude towards legislative activities of agents whose principals are undisclosed is revealed by statutes in many states requiring the registration of all lobbyists".

Public Utilities: Expenditures To Influence Public Opinion, 14 Cornell Law Quarterly 233, 233-234 (note).

Although the Board saw fit to ignore the circumstance, it might be noticed that the cases generally stress contingency of compensation as a sinister element in this class of contracts, *Noonan v. Gilbert*, 68 F. (2d) 775, and cases therein cited. The logic of this last position has been criticized in 14 Boston University Law Review 834 (note), above cited, but may, the writer should think, be justified on the ground that the necessary size of a contingent fee adds to the temptation of impropriety. Whatever, then, the ultimately

correct decision, it must be based on a repudiation of the Board of Tax Appeals theory of legitimacy.

The writer proceeds, then, on the assumption that the expenses here claimed deductible have met with the condemnation of every student, judicial or otherwise, of public affairs in a democracy, who has expressed his thoughts on the matter. Does that universal condemnation constitute a mandatory gloss of the adjectives "ordinary" and "necessary"? The writer thinks it does and he says further that the contrary view expressed by some judicial personalities rather shocks him. One of the latter speaking for the [fol. 89] majority of a divided court puts that position thus, "The revenue laws of the United States are not oversqueamish", *Alexandria Gravel Co. v. Commissioner*, 95 F. (2d) 615, 616. Well, as far as the writer is concerned they are. The writer suggests to the learned Circuit Judge above quoted that the Congress will probably not thank him for his somewhat gratuitous interpretation of their legislative morals. The writer may say that the learned Court seems to have had some of the very same qualms they refuse to attribute to Congress. Anyway, they weakened their own decision by naively asserting that the State Senator of Louisiana employed to sell "sand and gravel" to the Highway Commission of the "kingfish" domain did not exert any "personal influence" (he was undoubtedly employed because of his expert knowledge of geology).

The important word is, of course, ordinary. Although the cases,⁵ or most of them,⁶ stress the conjunctive character of the phrase, they are rather compelled to emasculate necessary, and for obvious reasons. After all, very few things (and very few people) are indispensable. The highest authority⁷ substitutes the milder "helpful" and certainly the practices in the case at bar were "helpful" to the respondent.

There are at least three possible methods of approach to a construction of the key adjective. They have all received judicial approval, but as they all, in the writer's

⁵ *Hubinger v. Comm.*, 36 F. (2d) 724; *Seufert Bros. Co. v. Lucas*, 44 F. (2d) 528; *Lloyd v. Comm.*, 55 F. (2d) 842, *Alexander Sprunt & Son, Inc. v. Comm.*, 64 F. (2d) 424; 4 Words & Phrases (5th Series) pp. 417-425.

⁶ *A. Harris & Co. v. Lucas*, 48 F. (2d) 187.

⁷ *Welch v. Helvering*, 290 U. S. 111.

judgment, lead to the same Rome of non-deductibility, it is not important here which one is adopted. As a matter of English, the word is thus defined, "customary or established order, general, customary, usual or normal, such as is commonly met with, of the usual kind, often, not above, or rather below, the average level of quality, commonplace", New Century Dictionary p. 1197. It is clear that the writer is not in a position to determine whether the present practice [fol. 90] is or is not a common occurrence in the American business world. The reported cases disapproving of the evil seem small in proportion to the extent of that world and the corresponding occasion for its exercise. That is, however, an unreliable guide as it does not take into account other factors which may have been producing causes. Testimony as to the reality of either the usual custom or the specific instance, although perhaps shameful, could like any other sad reality have been produced. A failure to offer the pleasanter evidence of an opposite tendency to a most ethical generosity cost the virtuous taxpayer his deduction in *Welch v. Helvering*, above cited.

A second interpretative test of ordinary is derived from the law of torts. The cases require the business act to be proximately caused, *Alexander Sprunt & Son v. Comm.*, above cited, *Comm. v. Continental Screen Co.*, 58 F. (2d) 625. In so doing they seem, at any rate, to be prescribing the requirement of foreseeability held essential to recovery in cases of indirect causation. That foreseeability in the writer's circumstance is, of course, the "reasonable contemplation of reasonable business men", 3 Paul & Mertens, *Law of Federal Income Taxation*, p. 46. This theory would seem to stem from some association of ideas. The word ordinary smacks of the average reasonable man and leads to the thought of the cognate proximate cause. It is probably as sensible to allow the deduction of foreseeable expenses as it is to allow recovery for foreseeable harm. It seems, nevertheless, a novel canon of statutory construction. The "reasonable contemplation of reasonable business men" like "reasonable care under the circumstances" sets up something of an imponderable standard. As juries and courts wrestle with the latter, so the courts must perhaps struggle with the former. To do so, they must be equipped with weapons in the shape of testimony and so under this test also the writer is confronted with the same failure of business proof he has already spoken of.

[fol. 91] The third angle of incidence is to the writer's way of thinking both the most satisfactory and most in accord with sound principles of legislative interpretation. It postulates an understanding of and a desire for the effective working of the democratic process on the part of all the organisms of that process. From that follows the assumption that any word capable of an interpretation consistent with the said effective working must receive such an interpretation and no other. And from that follows the further assumption that the Congress will be held to have intended to include in the word ordinary at minimum no practices falling below the standards to which the courts have given their own approval. In other words the courts will take for granted that the Congress did not intend to use a word capable of being stretched to cover acts which both it and the courts condemn and to benefit actors which both it and the courts refuse to help. Both Congress and the courts, as the writer has pointed out, have many times expressed their unfavorable opinion of these attempts to sell the pig of public welfare in the poke of public service. Mr. Justice Cardozo in *Welch v. Helvering*, above cited, with his usual felicity said, "The standard set up by the statute is not a rule of law; it is rather a way of life", 290 U. S. 111, 115. The writer refuses to sanction the Congressional way of life envisaged for the Congress by the Board of Tax Appeals.

So much for what the writer thinks to be principle. How much for what the petition claims to be the authority? Many more decisions than are cited in the briefs can be found in volume 3 of Paul & Mertens, *Law of Federal Income Taxation*. The learned authors thereof note the struggle that has shaken the courts in their efforts to arrive at what the writer is declaring to be the sound conclusion.

" * * * Underlying the whole question is the conflict between two major forces. On the one side is the desire to stultify or discourage criminal acts by denying the taxpayer [fol. 92] even incidental benefits therefrom as, for example, the deduction for income tax purposes of the expenses incurred in connection with the criminal act. This is the 'public policy' force. The conflicting force arises from the statutory warrant to deduct ordinary and necessary expenses of the business. One cannot predict with any degree of certainty the right to such deductions. If the act necessitating the expenditure is wholly tainted with criminality,

public policy prevails and the deduction is denied. On the other hand, if the act does no great violence, tested by the *mores* of the day, the Court may, sometimes by tortuous reasoning, emerge with a permission to deduct." 3 Paul & Mertens, Law of Federal Income Taxation, p. 44

Nevertheless, the weight of authority, if that is important, is on the writer's side. The cases both in the Board of Tax Appeals and in the courts are collected and collated in 3 Paul & Mertens, above cited, under the headings, Fines and Penalties § 23.45, Counsel Fees § 23.46, Cost of Legislative Representation: 'Lobbying' Fees § 23.47, and under the cognate titles, Charitable Contributions § 23.66, Gambling Expenses and Exchanges in Illegal Transactions § 23.156, Statutory Provision for Losses § 26.02, Nature of Organizations Which Are Exempt § 32.14. It is perhaps interesting to note that the same general problem has arisen under a somewhat similarly framed English statute,⁸ and that the cases appearing in 17 Halsbary's Laws of England (2d Ed.) pp. 152 et seq., seem to be in harmony with the ethical view for which the writer is contending. See *Inland Revenue Commissioners v. Warnes, & Co.*, 2 K. B. 444, *Inland Revenue Commissioners v. Von Glehn*, 2 K. B. 553. There is also one case in the Privy Council on Appeal from New Zealand wherein the expenditure denied deduction was by a brewery, for canvassing, advertising and printing directed to swaying the voters in a referendum on local option, *Ward [fol. 93] and Company Ltd. v. Conn.*, 1 English Law Reports, Appeal Cases, p. 145.⁹

The Board of Tax Appeals, in one sense, two Judges of this Court and other Judges of other courts, in another sense,¹⁰ stress the rule of administrative construction. They refer, of course, to Regulation 74, Article 262, which forbids

⁸ 8 & 9 Geo. 5, c. 40, Cases I & II, Sched. D, r. 3 (a).

⁹ Taxation—Income Tax—Corporations—Deductions From Gross Income For Charitable Contributions as Ordinary Business Expense, 30 Columbia Law Review 1211 (note); Taxation—Income Tax Deduction—Commercial Bribery as an "Ordinary and Necessary" Expense, 35 Columbia Law Review 125 (note); Taxation—Income—Deductibility of Counsel Fees Paid by Corporation in Defense of Prosecution, 17 Virginia Law Review 831 (note).

¹⁰ Vide *Sunset Scavenger Co. Inc.* 1. Comm., 84 F. (2d) 453.

any deduction, or at least a sort of quasi-charitable deduction, to corporations expending money "for lobbying purposes, the promotion or defeat of legislation, the exploitation of propaganda, including advertising other than trade advertising, and contributions for campaign expenses".¹¹ The writer of this opinion has little faith in this rule. He quite agrees with the learned author of an article in the *Yale Law Journal* who says:

"Among the innumerable fictions which have formed a part of the science of law, that which holds the record for unrealism is the doctrine that where a statute has been reenacted in the same form after an administrative construction, Congress has silently approved and incorporated the existing ruling. Our tax laws are reenacted so repeatedly that this rule is invoked more often than the general statement as to the validity of regulations standing alone. Unfortunately, the reenactment rule presumes an attention on the part of Congress in connection with tax legislation which is more ideal than real. The thought is that Congress, each time it passes a revenue act, has omniscience as to all outstanding regulations and judicial decisions and that it will be thoroughly diligent to correct by legislation any interpretation with which it disagrees. There follows the thought that inaction is action in that a failure to legislate implies [fol. 94] an agreement with all outstanding regulations, without any apparent distinction as to their interpretative or legislative character.

"Anyone cognizant of the processes and exigencies of tax legislation is perfectly familiar with the simple fact that any such presumption is not only artificial, but in large part unfounded. * * *"

Paul, *Use and Abuse of Tax Regulations in Statutory Construction*, 49 *Yale Law Journal* 660, 663-664.¹²

The writer finds no lack of logic in taxing income from illegal sources,¹³ and refusing a deduction for the same type of expenses. After all, the word applicable to one face of

¹¹ See 3 Paul & Mertens, above cited, § 23 56.

¹² cf. *The Supreme Court On Administrative Construction as a Guide in the Interpretation of Statutes*, 40 *Harvard Law Review* 469 (note).

¹³ *U. S. v. Sullivan*, 274 U. S. 259.

the medal, income, is the broadest possible, whereas the words applicable to the other have the many limitations the writer has tried to indicate. Further, the medal as a whole embodies policies and a probable Congressional intent which must have consistent application. Any discouragement of ill-gotten gains entails a corresponding lack of sympathy with the means of getting them. Thus everything the rascal takes in must be taxed, and as little as possible of what he expends must be exempted. In conclusion, the writer might note that the decision of the Board of Tax Appeals runs contrary to everything they have previously decided.¹⁴

[fol. 95] MARIS, Circuit Judge, dissenting.

I fully concur in the opinion of my brethren that this court consists of all five circuit judges in active service and that the court may lawfully sit en banc, as it did in this case. I find myself, however, unable to agree with the conclusion which the majority have reached as to the merits of the case for reasons which I shall state.

The taxpayer entered upon the business of seeking to bring about the return of its principals' seized property through the passage of Congressional legislation authorizing such return. Its compensation was to be contingent upon and measured by its success in securing the return of the property and it was to bear all the expenses of its effort. Among these expenses were substantial sums paid to Ivy Lee for publicity work, including the making of arrangements for speeches and speakers around the country and cooperating with the press in editorial comments, as well as news items, and to W. F. Martin and J. Reuben Clark for the preparation of propaganda concerning international relations, treaty rights, and the historical policy of the United States relative to enemy-owned property in times of war. It is these sums which the taxpayer seeks to deduct from its gross income as ordinary and necessary expenses of its business in computing its net income subject to income tax. The majority of this court deny the right to the deductions upon grounds, none of which, in my opinion, is valid.

¹⁴ Easton Tractor and Equipment Co. v. Comm., 35 B. T. A. 189; Mrs. William P. Kyne v. Comm., 35 B. T. A. 202; Alexandria Gravel Co. v. Comm., 35 B. T. A. 323.

Three of my brethren conclude that the Board of Tax Appeals erred in holding the deductions to be "ordinary" business expenses and therefore within the category of deductions permitted by the Revenue Act. As I understand it, they take the view that the expenses were not "ordinary" because they were paid in execution of a contract which was void as against public policy and because they were paid in an enterprise which was against public policy and which in any event did not meet the standard of morality in public affairs set by students of political science.

[fol. 96] Their conclusion that the contract between the taxpayer and its principals is against public policy is rested upon the decisions of the Court of Appeals of the District of Columbia in *Gesellschaft Fur Drahtlose Telegraphie M. B. H. v. Brown*, 78 F. 2d 410, and *Brown v. Gesellschaft Fur Drahtlose Telegraphie M. B. H.*, 104 F. 2d 227, holding void the provisions of a similar contract between alien claimants and an American agent which provided for the payment of compensation to the agent on a contingent basis. Those decisions were placed upon the ground that the Settlement of War Claims Act was "favor legislation" as distinguished from "debt legislation" and that a contract to procure "favor legislation" for a contingent fee is against public policy and, therefore, void. It was accordingly held that the agent might not recover the contingent fee stipulated for in the contract. I have grave doubt of the soundness of the distinction thus drawn between "favor legislation" and "debt legislation"¹ and I

¹ The distinction sought to be drawn, as I understand it, is between legislation designed to provide for or facilitate the settlement of existing claims against the government and legislation which confers benefits upon individuals who had no claims against the government prior to its passage. This distinction seems to have been first expressed by the Court of Appeals of the District of Columbia in the first *Brown* case, *supra*. I do not find the distinction referred to in any decision of the Supreme Court of the United States. On the contrary the rule of that court seems to be to strike down such contracts as against public policy if it appears to the court that they are likely to facilitate and encourage the corruption of the legislative body. *Trist v. Child*, 88 U. S. 441. If this is the test, as I think it is, it would seem

am clear that in any event the validity of the contract has no bearing on the question before us, for reasons which will be discussed later. But even if its bearing be conceded it seems to me that the Settlement of War Claims Act was in fact "debt legislation."

Section 7 of the Trading with the Enemy Act (50 U. S. C. A. Appendix § 7) authorized the seizure by the alien property custodian of enemy-owned property such as the [fol. 97] textile properties here involved, but it did not purport to confiscate these properties without return or compensation. On the contrary it clearly contemplated that the former owners had claims which would have to be dealt with after the war, for by Section 12 (50 U. S. C. A. Appendix § 12) the act provided that "After the end of the war any claim of any enemy or of an ally of enemy to any money or other property received and held by the alien property custodian or deposited in the United States Treasury, shall be settled as Congress shall direct." Here was not only the recognition of the existence of claims on the part of the former owners of seized property but also a clearly implied invitation to them to solicit from Congress legislation providing for the settlement of their claims. That the Settlement of War Claims Act which finally provided for these claims was "debt legislation" seems to me quite clear in the light of these circumstances.²

As I have already suggested, however, I think that even though the taxpayer's contract was void because in violation of a public policy which frowns upon the offering of a contingent compensation for procuring legislation, it does not follow that the expenses paid in carrying out the agency constituted by the contract were not ordinary busi-

to follow that "debt legislation," since it is ordinarily devoid of general public interest and, therefore, not subject to public scrutiny during the process of enactment, would provide a much greater opportunity for legislation corruption than "favor legislation" which ordinarily affects a larger section of the public and is, therefore, subject to much greater public attention while being considered by the legislative body.

² For cases in which contingent fee contracts have been upheld under similar circumstances see *Spalding v. Mason*, 161 U. S. 375; *Winton v. Amos*, 255 U. S. 373, and *Hollister v. Ulvi*, 199 Minn. 269, 271 N. W. 493.

ness expenses. The illegality suggested is as to the manner of compensation and not as to the result sought to be accomplished. It, therefore, seems to me to be wholly immaterial to the decision of the case before us whether the contract between the taxpayer and its principals was void because of the contingent fee for procuring what the majority describe as "favor legislation." The fact remains that the business contemplated by the contract was carried through, the contingent compensation was paid and is now being taxed, and the expenditures here sought to be deducted were expended in carrying on that business and earning that compensation. The alleged invalidity of the [fol. 98] contract obviously does not affect the taxability of the income and I see no basis for holding that it affects the deductibility of the expenses.

It is said by the majority that since the expenditures in question were made in execution of a void contract they "cannot be deemed to be ordinary. They are outside the norm of ordinary business conduct." It is also said that the solicitation of legislation, commonly known as "lobbying", is against public policy and has been condemned by judges and political scientists and that "the payment of moneys for carrying out a purpose contrary to public policy is by no means ordinary." As my colleague Judge Clark puts it in his concurring opinion the public policy, which he suggests prohibits "lobbying," must be read as a mandatory gloss upon the adjective "ordinary" in the statute. To me this is not interpretation but amendment of the legislative language. Section 23(a) of the Revenue Act of 1928 authorizes the deduction in computing net income of "all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business." The majority I think lose sight of the fact that the reference is to any trade or business. It seems obvious to me that the act contemplates that taxpayers will engage in all sorts of trades and businesses including businesses which are against public policy or even criminal in character, and that those expenses which are ordinary and necessary in each particular type of trade or business may be deducted from the income derived therefrom. The determination of the character of the expenses as ordinary and necessary is, therefore, not to be based, as the majority suggest, upon "the norm of ordinary business conduct" in general but is to be made in the light of the relation of the expenses to the

particular trade or business. As Mr. Justice Cardozo said in *Welch v. Helvering*, 290 U. S. 111, 113, "Now, what is ordinary, though there must always be a strain of constancy within it, is none the less a variable affected by time and place and circumstance."

[fol. 99] It seems to me that the majority by their decision are converting into a penal statute what was intended by Congress to be solely a revenue measure. The revenue laws, as Judge Sibley aptly said in *Alexandria Gravel Co. v. Commissioner*, 95 F. 2d 615, 616, "are not oversqueamish. By the broad definition of gross income, income arising from an illegal business is taxed even though the illegality be one declared by the Constitution itself. *United States v. Sullivan*, 274 U. S. 259, 47 S. Ct. 607, 71 L. Ed. 1037, 51 A. L. R. 1020. The provisions of the statute fixing the deductions to be regarded in arriving at the net income which alone is taxed, 26 U. S. C. A. § 23, are as broad and unqualified as those defining the taxable gross income." There is no suggestion in these provisions that the word "ordinary" is to be restricted in meaning to those expenditures only which are not against public policy or which meet a moral standard laid down by textwriters and courts. On the contrary it has been held that business expenses are deductible even though by reason of the nature of the business they involve payments so clearly criminal as bribes for "protection." *Steinberg v. United States*, 14 F. 2d 564. As Judge Hough demonstrated in the case cited the income tax law is not a penal statute but a revenue measure. It taxes income derived from criminal enterprises as well as those which the law countenances and its purpose is to tax the net income derived therefrom not the gross receipts.

In the present case the business upon which the taxpayer entered was that of soliciting through propaganda the passage of legislation, commonly known as "lobbying." This is an activity which Congress has never seen fit to prohibit which has always been freely indulged in without restraint. The facts stipulated in the record before us do not show that the taxpayer indulged in any questionable practices or that its activities in respect of which the expenses were incurred were against public policy. It was incumbent upon the government to show that the taxpayer's activities were illegal or against public policy if such was [fol. 100] the case. It failed to do so. Certainly this court

may not indulge the presumption, as I think the majority do, that the petitioner was guilty of improper conduct not disclosed by the record merely because it did not produce affirmative evidence of its innocence.

The question which we are called upon to determine is whether the Board of Tax Appeals was in error in finding as a fact that the activities for the cost of which the taxpayer seeks deduction were ordinary in the particular business in which it was engaged. As we have seen, the taxpayer engaged Ivy Lee to arrange publicity and Martin and Clark to prepare propaganda. I think it must be conceded that publicity and propaganda are methods of procuring legislative action which have been universally employed in this and every other democratic nation. Since the business in which the taxpayer was employed was that of soliciting legislation by Congress it seems to me to be entirely clear that expenditures for publicity and propaganda were "ordinary" in its particular line of business within the meaning of the Revenue Act. It is wholly beside the point to consider whether such expenditures would be ordinary in business generally. It is doubtless true that expenditures for lobbying activities are not ordinary in the case of persons engaged in mining, manufacturing or commercial businesses, but here lobbying was not merely incidental to the taxpayer's business but itself constituted the business. I do not understand that it is suggested that the taxpayer's expenses were not of the kind ordinarily incurred in the business of lobbying. To hold that these expenditures are not "ordinary" within the meaning of the Revenue Act because we think that they contravene that undefinable concept of the judicial mind which the courts have called "public policy," or because they are deemed to be unwise or improper by political scientists and judges seems to me to be reading into the Revenue Act what is not there. In doing so the majority have placed the stamp of illegality upon conduct which Congress has never declared to be criminal. [fol. 101] I think that in thus restricting the plain language of the act this court is exercising a legislative and not a judicial function. I cannot agree that we have such power.

Two of my colleagues suggest that the Board of Tax Appeals erred in finding that the expenditures in question were "necessary" business expenses because the activities which they represent cannot be shown to have been the proximate cause of the legislation enacted by Congress.

Their view is that only those expenses are necessary which result in achieving the object sought by the taxpayer for which the expenditures were incurred and that in this case the taxpayer's expenditures could not have been the proximate cause of the passage of the legislation sought since Congress must be presumed to have acted independently in the public interest. I cannot agree that the Revenue Act contemplates any such restriction upon the deductibility of business expenses. Certainly it has never heretofore been suggested that the deductibility of a business expense is contingent upon the success of the business enterprise in which it is incurred. So to hold would impose an intolerable burden upon taxpayer and Commissioner alike. Nor do I see any merit in the suggestion that the expense was not necessary because Congress must have acted independently not as a result of the taxpayer's activities. Mercantile advertising seems to me a perfect analogy. I do not think that my colleagues would go so far as to suggest that a merchant must be disallowed his trade advertising expenses because he cannot show that those expenses brought in customers or because he cannot show that the customers who did arrive came in under the hypnotic influence of his advertising and not in the exercise of an independent judgment in the light of their own self-interest. I entirely agree with Judge Clark that the word "necessary" as used in the act must be read as "helpful" and must be considered in the light of the enterprise in which the taxpayer is engaged rather than the result which it is seeking to achieve.

Finally two judges of the court take the ground that Article 262 of Regulations 74 prohibits the deduction of [fol. 102] expenses of the character involved in this case. I agree with the conclusion of the Board of Tax Appeals that this article of the regulations does not prohibit the deduction of these expenditures if they may fairly be classed as ordinary and necessary business expenses. The article in question is as follows:

"Art. 262. Donations by corporations.—Corporations are not entitled to deduct from gross income contributions or gifts which individuals may deduct under section 23 (n). Donations made by a corporation for purposes connected with the operation of its business, however, when limited to charitable institutions, hospitals, or educational institutions conducted for the benefit of its employees or their dependents are a proper deduction as ordinary and neces-

sary expenses. Donations which legitimately represent a consideration for a benefit flowing directly to the corporation as an incident of its business are allowable deductions from gross income. For example, a street railway corporation may donate a sum of money to an organization intending to hold a convention in the city in which it operates, with the reasonable expectation that the holding of such convention will augment its income through a greater number of people using the cars. Sums of money expended for lobbying purposes, the promotion or defeat of legislation, the exploitation of propaganda, including advertising other than trade advertising, and contributions for campaign expenses, are not deductible from gross income."

The article is arranged in the Regulations under Section 23 (n) of the Revenue Act. That section is entitled "Charitable and other contributions." It authorizes the deduction of such contributions in the case of an individual. By restricting deductions of this character to individuals the act denies them to corporations. I think that Article 262 was intended merely to be interpretive of Section 23 (n) [fol. 103] by making clear what that section leaves to inference, namely, that charitable and similar donations are not deductible as such by corporations and that lobbying and legislative expenses are likewise not deductible as such or in the guise of donations. The article was not intended to be interpretive of business expenses or to restrict the deduction of any expenditures which may fairly be deemed ordinary and necessary expenses of business under Section 23 (a) of the act. That this is so is borne out by the fact that Article 262 does not contain a cross-reference to Article 121 which does define business expense, while the latter, which states "As to items not deductible, see Section 24 and Article 281-284," does not contain a similar cross-reference to Article 262. Furthermore Article 262 itself points out that donations to charities may be deducted by a corporation as business expenses when made for purposes connected with the operation of its business.

The interpretation adopted by the majority would, it seems to me, render the article invalid as an invasion of the legislative power. Section 23 (a) of the Revenue Act authorizes the deduction of business expenses provided only that they are ordinary and necessary. Nowhere in the act is there any further qualification that they must not have

been incurred for lobbying or the promotion of legislation. Consequently the effect given to Article 262 of the Regulations, by the majority is, not to construe, interpret or implement an ambiguous, doubtful or general provision of the act, but rather to amend the unambiguous language of Section 23 (a) by adding to it a proviso to the effect that lobbying expenses shall not be deducted by a taxpayer even though they are ordinary and necessary in its business. It is settled that the law cannot thus be amended by regulation. *Koshland v. Helvering*, 298 U. S. 441; *Manhattan Co. v. Commissioner*, 297 U. S. 129. In *Koshland v. Helvering*, *supra*, Mr. Justice Roberts said (pp. 446, 447):

[fol. 104] "Where the act uses ambiguous terms, or is of doubtful construction, a clarifying regulation or one indicating the method of its application to specific cases not only is permissible but is to be given great weight by the courts. And the same principle governs where the statute merely expresses a general rule and invests the Secretary of the Treasury with authority to promulgate regulations appropriate to its enforcement. But where, as in this case, the provisions of the act are unambiguous, and its directions specific, there is no power to amend it by regulation. Congress having clearly and specifically declared that in taxing income arising from capital gain the cost of the asset disposed of shall be the measure of the income, the Secretary of the Treasury is without power by regulatory amendment to add a provision that income derived from the capital asset shall be used to reduce cost."

In *Sunset Scavenger Co. v. Commissioner*, 84 F. 2d 453, the Circuit Court of Appeals for the Ninth Circuit had under consideration the effect to be given to Article 262 of the Regulations. It held that this Regulation limited the sweeping terms of the statute by entirely prohibiting the deduction of lobbying expenses. This holding was based upon its conclusion that "the statute is ambiguous because it makes no determination of what is or is not an 'ordinary and necessary' expense." But what is "ordinary" or "necessary" as a business expense is clearly a question of fact to be determined in the light of the particular business in which the taxpayer is engaged. The words do not create an ambiguity but merely call for the exercise of the fact finding function. To permit the Commissioner of Internal Revenue to limit the scope of these words must necessarily

involve authorizing him "to convert what in the view of the statute is a question of fact requiring proof into a conclusive presumption which dispenses with proof and pre-[fol. 105] cludes dispute," to use the words of Mr. Justice Sutherland in *Miller v. United States*, 294 U. S. 435, 440. To continue in his words: "This is beyond administrative power. The only authority conferred, or which could be conferred, by the statute is to make regulations to carry out the purposes of the act—not to amend it." I am, therefore, not persuaded by the opinion of the court in the *Sunset Scavenger Co.* case that Article 262 should be given the broad construction which ~~the majority~~ my colleagues have placed upon it.

I am authorized to say that Judge Goodrich concurs in this dissent.

A true Copy:

Teste:

— — —, Clerk of the United States Circuit Court
of Appeals for the Third Circuit.

[fol. 106] IN THE UNITED STATES CIRCUIT COURT OF APPEALS
FOR THE THIRD CIRCUIT, TERM, 1939

No. 7056

COMMISSIONER OF INTERNAL REVENUE, Petitioner,

vs.

TEXTILE MILLS SECURITIES CORPORATION, Respondent

Appeal from the United States Board of Tax Appeals.

This cause came on to be heard on the transcript of record from the United States Board of Tax Appeals, and was argued by counsel.

On consideration whereof, it is now here ordered, adjudged, and decreed by this Court that the decision of the said Board of Tax Appeals in this cause be, and the same is hereby reversed, and the cause is remanded to the said Board of Tax Appeals with the direction to redetermine the tax in accordance with the view expressed by the majority of this court.

John Biggs, Jr., Circuit Judge.

Philadelphia, December 7, 1940.

[fol. 107] Stamp: Received & Filed, Dec. 27, 1940. William P. Rowland, Clerk.

IN THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE
THIRD CIRCUIT

No. 7056

COMMISSIONER OF INTERNAL REVENUE, Petitioner,

vs.

TEXTILE MILLS SECURITIES CORPORATION, Respondent

Respondent's Motion for Judgment

The respondent respectfully moves for the entry of a judgment affirming the decision by the Board of Tax Appeals, said judgment to be ordered by a circuit court of appeals comprising Judges Maris and Goodrich as a quorum of two judges in a circuit court of appeals as prescribed by Section 117 of the Judicial Code.

The reasons or grounds for this motion are as follows:

By Section 1141 (a) of the Internal Revenue Code:

"The Circuit Courts of Appeals * * * shall have exclusive jurisdiction to review the decisions of the Board, [fol. 108] except as provided in section 239 of the Judicial Code, as amended * * * and the judgment of any such court shall be final, except that it shall be subject to review by the Supreme Court of the United States upon certiorari, in the manner provided in section 240 of the Judicial Code, as amended * * *."

By Section 1141 (c) (1) of the Internal Revenue Code:

"Upon such review, such courts shall have power to affirm or, if the decision of the Board is not in accordance with law, to modify or to reverse the decision of the Board, with or without remanding the case for a rehearing, as justice may require."

By Section 1142 of the Internal Revenue Code:

"The decisions of the Board rendered after February 26, 1926 * * * may be reviewed by a Circuit Court of Appeals * * * as provided in section 1141, if a petition for such review is filed by either the Commissioner or the

taxpayer within three months after the decision is rendered * * *.”

By Section 1140 of the Internal Revenue Code:

“The decision of the Board shall become final—

“(b) (1) Upon the expiration of the time allowed for filing a petition for certiorari, if the decision of the Board has been affirmed or the petition for review dismissed by the Circuit Court of Appeals and no petition for certiorari has been duly filed * * *.

“(2) Upon the denial of a petition for certiorari, if the decision of the Board has been affirmed or the petition for review dismissed by the Circuit Court of Appeals * * *.

“(c) (2) If the decision of the Board is modified or reversed by the Circuit Court of Appeals, and if (1) the time [fol. 109] allowed for filing a petition for certiorari has expired and no such petition has been duly filed, or (2) the petition for certiorari has been denied, or (3) the decision of the Court has been affirmed by the Supreme Court, then the decision of the Board rendered in accordance with the mandate of the Circuit Court of Appeals shall become final on the expiration of 30 days from the time such decision of the Board was rendered * * *.”

By R. S. Section 1008 as amended (Section 350, Title 28, U. S. Code Annotated):

“No * * * writ of certiorari intended to bring any judgment or decree before the Supreme Court for review shall be allowed or entertained unless application therefor be duly made within three months after the entry of such judgment or decree * * *.”

By Section 240 Amended of the Judicial Code:

“(a) In any case, civil or criminal, in a circuit court of appeals * * * it shall be competent for the Supreme Court of the United States, upon the petition of *any party thereto*, whether Government or other litigant, to require by certiorari, either before or after a judgment or decree by such lower court, that the cause be certified to the Supreme Court for determination by it with the same power and authority, and with like effect, as if the cause had been brought there by unrestricted writ of error or appeal.” (Underlining added.)

In the matter at bar, wherein the respondent was forced before "a circuit court of appeals" by the petition for review filed by the petitioner, reviews of the Board decision have been had by two or more circuit courts of appeals presiding within the Third Judicial Circuit through decision rendered December 7, 1940, whereby one or more of said courts has rendered decision for the affirmance of the Board decision and one or more others of said courts has rendered decision for the reversal of the Board decision.

The respondent, acting within its rights, desires to apply for certiorari with reference to the decision of the Circuit Court of Appeals affirming the decision of said Board and comprising Judges Maris and Goodrich as a quorum of said Court of three judges prescribed by the Judicial Code, and will predicate its petition upon the existence of conflicting decisions by two Circuit Courts of Appeals within the Third Judicial Circuit and in the same case,—to wit, the case at bar,—as well as the importance of the question and the conflict of both decisions with the views expressed in Circuit Courts of Appeals within other judicial circuits.

However, the respondent stands barred of its right to so petition the Supreme Court for certiorari, except as a "judgment or decree" is rendered by said Circuit Court of Appeals comprising Judges Maris and Goodrich as a quorum of said Court.

Nor does the respondent possess the right to petition for certiorari prior to the entry of a judgment or decree, by [fol. 111] reason of the restrictions imposed in said R. S. 1008 to such an application being made "prior to the hearing and submission in that court," and the fact that such hearing and submission occurred not later than July 1, 1940.

Therefore, it is essential to the ends of justice in the respondent's prosecution of its statutory right, that the Circuit Court of Appeals comprising Judges Maris and Goodrich as a quorum of said Court do order the entry of a judgment in affirmance of the Board decision, and the respondent so moves for such a judgment.

Respectfully submitted, Textile Mills Securities Corporation, Respondent, by Edmund S. Kochersperger, 811 Investment Building, Washington, D. C., Attorney for Respondent.

[fol. 112] IN THE UNITED STATES CIRCUIT COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 7056

COMMISSIONER OF INTERNAL REVENUE, Petitioner,

vs.

TEXTILE MILLS SECURITIES CORPORATION, Respondent

Before Maris and Goodrich, Circuit Judges

The motion of the respondent for the entry of a judgment affirming the decision of the Board of Tax Appeals in the above entitled case is denied.

Albert B. Maris, United States Circuit Judge; Her-
bert F. Goodrich, United States Circuit Judge.

January 3, 1941.

[fol. 113] UNITED STATES OF AMERICA,
Eastern District of Pennsylvania,
Third Judicial Circuit, Set:

I, Wm. P. Rowland, Clerk of the United States Circuit Court of Appeals for the Third Circuit, Do Hereby Certify the foregoing to be a true and faithful copy of the original Transcript of Record and proceedings in this court in the case of Commissioner of Internal Revenue, Petitioner, vs. Textile Mills Securities Corporation, Respondent (No. 7056), on file, and now remaining among the records of the said Court, in my office.

In Testimony Whereof, I have hereunto subscribed my name and affixed the seal of the said Court, at Philadelphia, this 25th day of February in the year of our Lord one thousand nine hundred and forty-one and of the Independence of the United States the one hundred and sixty-fifth.

Wm. P. Rowland, Clerk of the U. S. Circuit Court
of Appeals, Third Circuit. (Seal.)

[fol. 114] SUPREME COURT OF THE UNITED STATES

ORDER ALLOWING CERTIORARI—Filed March 31, 1941

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Third Circuit is granted.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

Endorsed on Cover: File No. 45,161, U. S. Circuit Court of Appeals, Third Circuit, Term No. 812. Textile Mills Securities Corporation, Petitioner, vs. Commissioner of Internal Revenue. Petition for a writ of certiorari and exhibit thereto. Filed March 5, 1941, Term No. 812 O. T. 1940.

(3811)

IN THE
Supreme Court of the United States

OCTOBER TERM 1940.

No. ~~842~~ 34

TEXTILE MILLS SECURITIES CORPORATION, *Petitioner,*

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent.*

**PETITION FOR A WRIT OF CERTIORARI TO THE
UNITED STATES CIRCUIT COURT OF APPEALS
FOR THE THIRD CIRCUIT.**

EDMUND S. KOCHERSPERGER,

Counsel for the Petitioner,

811 Investment Building,
Washington, D. C.

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IN THE
Supreme Court of the United States

OCTOBER TERM 1940.

No.

TEXTILE MILLS SECURITIES CORPORATION, *Petitioner,*

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent.*

**PETITION FOR A WRIT OF CERTIORARI TO THE
UNITED STATES CIRCUIT COURT OF APPEALS
FOR THE THIRD CIRCUIT.**

The petitioner prays that a Writ of Certiorari issue to review the judgment or decree of a Circuit Court of Appeals for the Third Circuit entered in the above case on December 7, 1940, (R. 99) reversing a decision of the United States Board of Tax Appeals, and the denial of a motion for judgment by a different Circuit Court of Appeals for the Third Circuit on January 3, 1941, (R. 103) refusing to order a judgment affirming the said decision of the United States Board of Tax Appeals which had been rendered in favor of the petitioner.

Opinions Below.

Three opinions (R. 66 to 99) by Judges within the Third Judicial Circuit are expected to be reported in 116 Fed. (2d) The Board decision (R. 21-35) is reported in 38 B. T. A. 623. (Opinions below not yet reported)

Jurisdiction.

A judgment of a circuit court of appeals for the Third Circuit was entered December 7, 1940. (R. 99) The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925.

Questions Presented.

1. Whether certain expenses incurred by the petitioner under contract commitments in connection with the presentation of claims to Congress on behalf of former enemy aliens for the procurement and enactment of amendatory legislation authorizing the payment of the claims, are deductible by the petitioner in the ascertainment of taxable net income under the Revenue Act of 1928.

2. Whether a decision by the Board of Tax Appeals in favor of the petitioner has been both affirmed and reversed by a circuit court of appeals, so as to leave uncertain and in doubt the finality of decision by said Board within the meaning of pertinent statutes of the United States.

3. Whether the two judges of the Third Judicial Circuit who concurred in opinion for the affirmance of said Board decision in favor of the petitioner, were precluded from ordering a judgment of affirmance because bound by the opinions of the three other judges who opposed their views in that same judicial circuit, where all five of said judges purported to sit as a circuit court of appeals of five judges instead of a court of three judges as prescribed by the Judicial Code, Section 117; or, alternatively, whether the

views of said two judges constitute a judgment or decree of a circuit court of appeals in affirmance of said Board decision.

4. Whether the opinion concurred in by a quorum of two judges of the circuit court of appeals for the Third Circuit, agreeing for an affirmance of said Board decision, legally constitutes an affirmance of that decision so as to render said Board decision "final" within the meaning of Internal Revenue Code, Section 1140, if the respondent shall fail to file a petition for certiorari or, filing such petition, the same shall be denied by this Court.

5. Whether the decision of said Board, concurred in by two of the judges of the Third Judicial Circuit, should be affirmed as being founded upon correct statements of legal principles, or for reasons otherwise should be reversed.

6. Whether a "court en banc" when legally constituted within a judicial circuit, can omit from inclusion among the judges who sit as such court, the Associate Justice who has been assigned to that judicial circuit as Circuit Justice, the Chief Justice, or a District Judge.

7. Whether a circuit court of appeals can reach a conclusion adverse to a party-litigant in a case before the Board of Tax Appeals, by a disregard of the facts as agreed to by those parties and as found to be the facts by the Board.

8. Whether a majority of three judges out of five judges within the Third Judicial Circuit, are authorized to approve by their conclusions a shift by the respondent to a ground which the taxpayer had every reason to think was abandoned in the earlier stage of the litigation before the Board of Tax Appeals.

9. Whether the five judges who purported to render judgment of reversal of the Board decision by a three to two majority constituted a circuit court of appeals within the meaning of the Judicial Code and other pertinent statutes.

10. Whether the reenactment of the revenue-laws as to "ordinary and necessary expenses" deduction, constitutes a Congressional approval of the application of an Article in the Regulations dealing with "Donations by Corporations", as being pertinent to the Congressional intention in the language "ordinary and necessary expenses".

Statutes and Regulations Involved.

The statutes and regulations involved will be found in the Appendix, *infra*, pp. 21 to 23.

Statement.

After the termination of the War of 1914-1918 by Presidential Proclamation in 1921, and after efforts by the German Foreign Office with our Department of State had failed to procure the settlement of claims by former enemy aliens for the seizure and detention of their properties under the Trading With The Enemy Act, the services of the petitioner were engaged by certain of the former enemy aliens for the procurement from Congress of an Act of Congress that would accord a settlement of their claims. (R. 21-27; 47-54)

Section 12 of the Trading With The Enemy Act (which authorized the seizures of enemy properties) stated:

"after the end of the war any claim of any enemy or of an ally of enemy to any money or other property received and held by the Alien Property Custodian or deposited in the United States Treasury shall be settled as Congress shall direct." (R. 33.)

The Treaty of Berlin, restoring friendly relations with Germany, incorporated into the Preamble portions of the Joint Resolution of Congress of July 2, 1921, prescribing in part:

"All property of . . . German nationals . . . shall be retained by the United States of America and no disposition thereof made, except as shall have been heretofore or specifically hereafter shall be provided by law

until such time as the Imperial German Government . . . shall have . . . made suitable provision for the satisfaction of all claims against said Governments . . . of all persons . . . who owe permanent allegiance to the United States of America and who have suffered through the acts of the Imperial German Government. . . .”

The Settlement of War Claims Act of 1928 was enacted March 10, 1928 with title as follows:

“AN ACT To provide for the settlement of certain claims of American nationals against Germany, Austria, and Hungary, and of nationals of Germany, Austria, and Hungary against the United States, and for the ultimate return of all property held by the Alien Property Custodian.”

The petitioner performed the services required by its contracts in the procurement from Congress of that Settlement of War Claims Act of 1928, and was authorized by its charter for such an undertaking. (R. 49-55.)

The contracts between the petitioner and the former enemy aliens provided for compensating the petitioner upon a contingent fee basis, and also required that the petitioner bear and pay all of the expenses in performance of the services in procurement of the Act of Congress. (R. 52, 53)

In filing its tax-returns the petitioner included the commissions within gross-income and claimed deductions for the expenses which it had incurred in connection with procuring the Act of Congress. (R. 8, 20, 14-18.)

The alleged tax-deficiency results wholly from a disallowance of such expenses. (R. 14-18.)

When the case was presented to the Board, the respondent's sole contention was, that even though the expenses were “ordinary and necessary” nevertheless they were not deductible because they related to “sums of money expended for lobbying purposes, the promotion or defeat of legislation, the exploitation of propaganda” within the meaning of Article 262 of Regulations 74, which had as its title

"Donations by Corporation". (R. 28) Article 121 of Regulations 74 covered the subject of "ordinary and necessary expenses", and made no mention or reference to the Article 262.

The case was submitted to the Board upon an Agreed Statement of Facts or Stipulation, (R. 47-59) wherefrom the Board was justified in its statement by opinion as follows:

"Accordingly, we are unable to reach any conclusion except that the expenses here in question were in fact 'ordinary and necessary' in the conduct of petitioner's business and, having reached that conclusion, it is our opinion that the statute directs their allowance as deductions in determining petitioner's net income." (R. 34)

The Board also stated:

"The respondent has made no claim, as we have pointed out, that such employment was outside the scope of petitioner's powers or business and we have concluded from the record that the services rendered were necessary for the accomplishment of the desired result. There has been no showing that the petitioner indulged in any questionable practices in carrying out the purposes of its employment and no showing or claim that the activities in respect of which the expenses were incurred were against public policy." (R. 33)

In Petition for Review to the Third Judicial Circuit the respondent, for the first time, raised the contention through Assignment of Errors that the expenses were not "ordinary and necessary". (R. 42.)

Effective March 1, 1940, the judges of the Third Judicial Circuit amended the Rules for that Circuit, Rule 4 providing:

"CONSTITUTION OF THE COURT. QUORUM

- 1. The Court—Judges Who Constitute It—Number of Judges To Sit.

The court consists of the circuit justice, when in attendance, and of the circuit judges of the circuit who are in active service. District judges and retired circuit judges of the circuit sit in the court when specially designated or assigned as provided by law. Three judges shall sit in the court to hear all matters, except those which the court by special order directs to be heard by the court *en banc*.

2. Quorum—. . .

Two judges shall constitute a quorum. . . ."

By a special order the argument of the case was directed to be held before the court "*en banc*". The argument occurred on July 1, 1940 before Judges Biggs, Maris, Clark, Jones, and Goodrich, (R. 66) but Mr. Justice Roberts did not attend the argument nor did he thereafter participate in opinions or decision or judgment, nor did the Chief Justice or a District Judge participate.

On December 7, 1940 three sets of opinions were enunciated. Judge Biggs rendered an opinion for reversal of the Board decision for certain stated reasons, with which Judge Jones concurred. (R. 66) Judge Maris rendered an opinion for affirmance of the Board decision for certain stated reasons, with which Judge Goodrich concurred. (R. 90) Judge Clark rendered an opinion for reversal of the Board decision for certain stated reasons, with which none of the other judges concurred. (R. 82)

All five of the judges, having approved the changes by Rule 4, agreed that the Circuit Court of Appeals for the Third Circuit was authorized to sit by five judges, instead of the three judges prescribed by Judicial Code, Section 117. (See opinions, R. 66 to 99)

After knowledge of the prejudicial action through a three-to-two holding by a court in excess of three judges prescribed by the Judicial Code, the petitioner filed a Motion for Judgment addressed to Judges Maris and Goodrich as constituting a "quorum of two judges" in a circuit court of appeals, (R. 100) as stated both in the Rule 4 and in

the Judicial Code. That Motion was denied January 3, 1941 by a circuit court of appeals comprising Judges Maris and Goodrich as a quorum of two judges. (R. 103) That Motion demanded, as a matter of right, the entering of a judgment by a circuit court of appeals for the Third Circuit, affirming the decision by the Board which held in favor of the petitioner. (R. 100)

In only one regard can the petitioner's counsel find a degree of harmony or agreement on the part of the reasons that actuated Judge Clark to a disagreement with the Board and an agreement with Judges Biggs and Jones,—namely, with reference to the point that the Respondent did not raise before the Board but raised for the first time by Assignment of Errors in the Petition for Review.

It was the opinion expressed by those three Judges Biggs, Clark, and Jones, that under no circumstances or facts could such expenses be deemed "ordinary and necessary", because they involved the procurement of an Act of Congress (R. 66 to 82).

The other reasons assigned in the opinion of Judge Biggs, renders a situation where two judges stood in agreement regarding those reasons for a reversal, while two other Judges, Maris and Goodrich, expressly and directly disagreed with those two of their colleagues, and with the separate reasons of Judge Clark as well. Judge Clark does not appear to have agreed with those other reasons expressed in the opinion of Judge Biggs.

The matter thus stands in a situation where two Circuit Judges, Maris and Goodrich, agreed with the majority of Board-Members, and the three other Circuit Judges agreed only with respect to an issue that had not been controverted or disputed before the Board, and such a situation of divergent views among five judges evidences the greater possibility for a lack of uniformity by a court "en banc" if engaged in by such circuits as the Sixth and Ninth where seven Circuit Judges are authorized to sit.

Specification of Errors to be Urged.

1. A circuit court of appeals comprising Judges Maris and Goodrich as a quorum of two judges in a court of three judges specified by Judicial Code, Section 117, erred in refusing to order an entry of judgment of affirmance of the Board decision, as demanded by petitioner's Motion for Judgment.

2. The judgment of reversal of the Board decision is invalid because rendered as the action by a majority of five judges, instead of by a court of three judges as specifically provided by the Judicial Code, Section 117 and by the other pertinent provisions of that Code.

3. The alleged court en banc was illegally constituted, since it did not include within its membership the Associate Justice who was assigned as a Circuit Justice to the Third Judicial Circuit, nor the Chief Justice, nor a District Judge of the Circuit.

4. The circuit judges of the Third Judicial Circuit erred in holding and deciding that these judges, to the exclusion of the Circuit Justice holding assignment to that judicial circuit, the Chief Justice or a District Judge, can sit and decide a case as a "court en banc" in a situation (such as in the case at bar) where decisions within that circuit do not stand in a state of conflict and where the decision in the specific case would not stand in conflict with any prior decision within that circuit.

5. The Rule 4 of the Third Judicial Circuit, by authority of which the five judges purported to decide the case at bar by a majority of three judges to two judges, violates Article III, Section 1, of the Constitution of the United States, for the reason that a five-men court is not a part of "such inferior Courts as the Congress may from time to time ordain and establish", and to the contrary the Congress has prescribed a circuit court of appeals as a three-men court.

6. Any set up of five judges into a validly constituted circuit court of appeals of three members wherein any two of Judges Biggs, Clark, and Jones comprised a quorum of two judges, erred in holding and deciding that, collectively or alternatively:

(a) Petitioner's contracts were invalid or void as being against public policy.

(b) The facts as agreed upon between the parties and as found to be the facts by the Board, can be disregarded as the facts, and an adverse decision be rendered upon a different assumption of the facts, as made by such a quorum of judges.

(c) Petitioner's contracts or services sought the enactment of "favor legislation", as distinct from "debt legislation".

(d) The Trading With The Enemy Act did not in itself create "debt legislation".

(e) The Settlement of War Claims Act of 1928 was not in settlement of claims that Congress recognized to be existent by the expressed provisions of the Trading With The Enemy Act.

(f) The petitioner's expenses were not ordinary and necessary expenses within the construction of the Revenue Act of 1928.

(g) There is a conclusive and un rebuttable presumption of law that every contract requiring the performance of services for the procurement of "favor legislation" is improper, inferentially fraudulent or wrongful, and basically void as being against public policy, regardless of the contrary statement by the Board that no such issue was presented in the case before the Board.

(h) The opinion of Judge Maris, concurred in by Judge Goodrich, did not express the correct legal principles as the basis for a judgment affirming the Board decision.

(i) The circuit court of appeals can depart from the accepted and usual course of judicial proceedings, by reversing the Board on an issue that was not raised in the Board and wherein the advancing of the issue by the respondent for the first time within a circuit court of appeals represents a shift to a ground which the taxpayer had every reason to think was abandoned in the earlier stage of the litigation when before the Board.

(j) The cause should be remanded to the Board with the direction to redetermine the tax in accordance with the view expressed by the majority, and without according the petitioner any opportunity for the presentation of additional evidence material to the new issue first raised by the court itself in the opinions of Judges Biggs and Clark.

(k) That Congress, by the reenactment of the revenue laws without change in the language for deduction of "ordinary and necessary expenses", is to be presumed as having approved Article 262 of Regulations 74 (dealing with the subject "Donations by Corporations"), just as if that Article had been incorporated into Article 121 (which dealt specifically with "ordinary and necessary expenses"), although neither Article made the slightest specific reference to the other Article, and further, that Congress is to be presumed by such reenactment to have given its approval to an interpretation which the Bureau, for the first time, makes *in the very case at bar*.

(l) The ordering of a judgment of reversal of the decision of the Board of Tax Appeals.

7. If the court of five judges constitutes a validly composed circuit court of appeals for the Third Circuit, the court erred in holding and deciding relative to all of the grounds set forth herein under subdivision 6, (a) to (l) inclusive.

8. Although no statute or law enacted by Congress prohibited any of the actions engaged in by the petitioner in

performance of its contract obligations, the holding by Judges Biggs, Jones and Clark, converts without authority of law, the revenue-laws into a penal statute imposing a fine levied upon the petitioner's gross receipts because the petitioner engaged in a valid, legal, and unprohibited business undertaking which those judges personally did not favor, the holding in that regard constituting unconstitutional judicial legislation as an unauthorized assumption of the powers conferred by the Constitution upon the Congress.

Reasons for Granting the Writ.

1. The holding by the majority of three judges, that the expenses incurred in services under a void or illegal undertaking are not allowable deductions in the ascertainment of taxable net income, is directly in conflict with decisions of other courts, of the Board, and of the Treasury Department's own Rulings:

Steinberg v. United States, 14 Fed. (2d) 564 (2d C. C. A.)

Alexandria Gravel Co, Inc. v. Commissioner, 95 Fed. (2d) 615 (5th C. C. A.)

Sullivan v. United States, 15 Fed.(2d) 809, 810 (4th C. C. A.) (Reversed on other grounds, 274 U. S. 259)

Helvering v. Hampton, 79 Fed.(2d) 358 (9th C. C. A.)

McKenna v. Commissioner, 1 B. T. A. 326

Frey v. Commissioner, 7 B. T. A. 338

Terrell v. Commissioner, 7 B. T. A. 773, 776

Bureau Ruling, IT 2175, Cumulative Bulletin IV-1-141

Bureau Ruling, S. M. 4078, Cumulative Bulletin V-1-226 (cited with approval in *Kornhauser v. United States*, 276 U. S. 145, 153)

Additionally, that question is submitted as being "an important question of federal law which has not been, but should be settled by this court" (Rule 38, 5(b), Rules of this Court).

2. The holding by opinion of Judge Biggs, that the petitioner's contracts for the procurement of an Act of Congress and services connected therewith, were void as being against public policy, is in conflict with decisions by this Honorable Court and also with decisions in other courts.

Winton v. Amos, 255 U. S. 373, 393.

Steele v. Drummond, 275 U. S. 199; 11 Fed.(2d) 595 aff'd.

Lucas v. Wofford, 49 Fed.(2d) 1027 (5th C. C. A.)
(See, *Spalding v. Mason*, 161 U. S. 375)

3. The basing of their decision for the reversal of the Board decision by Judges Biggs, Jones, and Clark, upon the new issue involving "ordinary and necessary expenses", which had not been contested in the Board, represents a departure by the court "from the accepted and usual course of judicial proceedings", for which reason this Court granted certiorari in *Helvering v. National Grocery Company*, 304 U. S. 282, under Rule 38, 5(b), as involving a situation requiring the supervision by this Court, and the Rule is invoked for similar reasons here.

4. The single ground of unanimity by the majority of three judges out of five, is found solely by a "shift to ground which the taxpayer had every reason to think was abandoned in the earlier stages of this litigation" (quoting from *Helvering v. Wood*, 309 U. S. 344), which clearly appears upon a mere reading of the Stipulation of Facts (R. 47-59) and the Board's findings and opinion (R. 21-35) (Rule 38, 5(b), concluding clause, is suggested as being applicable).

5. The opinions by Judges Biggs and Clark, finding as their common ground for reversal of the Board decision (concurring in by Judge Jones as to reasons stated by Judge Biggs only), the conclusive and irrefutable presumption as to illegality both as to the contracts and the petitioner's actions, not only denying to the petitioner all right to prove the facts in the Board but also disregarding the facts to the contrary as agreed upon by the parties and found to be

the facts by the Board, would evidence a grave miscarriage of justice unless consideration be accorded by this Court, constituting a precedent against all taxpayers generally.

6. The holding by opinion of Judge Biggs, that the determination of deductibility as "ordinary and necessary expenses" is not a question of fact in relation to the business on which the taxpayer was engaged, is contrary to the decisions by this Court, as well as to the overwhelming weight of authority.

Welch v. Helvering, 290 U. S. 111.

Kornhauser v. United States, 276 U. S. 145.

Also, cases cited under 1st subdivision above of "Reasons".

7. The holding by opinion of Judge Biggs, concurred in by Judge Jones as a "quorum", that whether expenses are "necessary" depends upon the establishment by proof of a proximate causation between the incurrence of the expense and the end sought to be accomplished by the expenditure, is so original as to revolutionize all previous interpretations of the language "ordinary and necessary expenses", and emphasizes such extreme importance to every business in the United States, relative to the determination of income taxes, (the Treasury Department as well), as to merit consideration and decision by this Court by way of clarification on such an important subject.

8. The holding by opinion of Judge Biggs regarding the effect of Article 262 of Regulations 74 by reason of the reenactment of the revenue-laws as to deduction of "ordinary and necessary expenses", in a situation where said Article 262 related to the specific subject of "Donations by Corporations" and an entirely different Article dealt with the subject of deductible expenses (without any cross-reference), represents such a startling and original extension of the doctrine of "legislative approval", as to merit the consideration by this Court in a clarification of such an important subject, as finds recent comment in various Law Reviews:

"Regulations, Reenactments, and the Revenue Act", 54 Harvard Law Review 377.

"A Summary of the Regulations Problem", 54 Harvard Law Review 398.

"Use and Abuse of Tax Regulations in Statutory Construction, 49 Yale Law Journal 660.

"Treasury Regulations and the Wilshire Oil Case", 40 Columbia Law Review 252.

"The Scope and Effect of Treasury Regulations, etc." 88 University Of Pennsylvania Law Review 556.

Paul, "Studies in Federal Taxation", Third Series, 420.

8. The holding by opinion of Judge Biggs, concurred in by Judge Jones, converts the revenue-laws into a penal statute, without authority or precedent, and thus presents an original important question of law which never has been decided by this Court, but which merits this Court's consideration. See, opinion by Judge Maris in this case, and comment upon this case in Harvard Law Review, February 1941, Vol. 54, pages 698, 699.

9. The questions presented in this case have an importance, not merely to the petitioner, but to all taxpayers in general, because our Country now approaches high tax rates and actions similar to those prevailing during 1914-1918; within the past year the Defense Program stood inactive, until contracting-companies and Congress found agreement upon satisfactory legislation for charging off the amortization of defense facilities against income and, necessarily, expenses had to be incurred by the companies in the solicitation of such "favoring legislation" from Congress; many other situations of remedial legislation are certain to occur, from claims arising of defense-contracts and otherwise; with corporations at present facing maximum taxation of 24 per cent as a normal tax, 50 per cent as an excess-profits tax, and 12 per cent as a declared-

value excess profits tax, (with certainty of higher rates by legislation soon to be enacted), it is of particular importance that taxpayers know whether or not their expenses in soliciting Congress for remedial legislation are, or are not, to bear taxation, and the extent to which their actions shall be deemed proper under the First Amendment to the Constitution:

“Congress shall make no law respecting . . . the right of the people . . . to petition the Government for a redress of grievances.”

In the case at bar, it should be noted, neither the petitioner nor its agents engaged in any conduct that was, to the slightest degree improper. The majority of judges impose “taxes” upon our gross receipts, without deduction for our expenses, solely because we entered upon contracts to obtain an Act of Congress in settlement of claims and honestly performed our contract obligations.

The Settlement of War Claims Act was not a mere matter of “legislation” in the ordinary sense of the term. It represented a compromise as between the representatives for the respective claimants, Germans against the United States and Americans against Germany. House Report No. 17, 70th Congress, 1st Session, at page 4, succinctly stated the situation:

“. . . these parties and their representatives voluntarily got together and agreed upon the concessions to be made by each. The present bill proposes to carry out this agreement.”

The “agreement”, however, came only after a long contest throughout the Country, whereby the American-claimants sought the confiscation of the Germans’ properties as represented in possession of the Alien Property Custodian, and the properties had to be preserved from such confiscation by the Germans’ representatives meeting argument *with* argument. That was the sole and only reason for the petitioner’s expenses in question. But the agreement

finally came and with it the Act of Congress. We direct attention to the Stipulation, Record p. 49 et seq :

“6. The obligations of the petitioner under the afore-said representation contracts were such as *necessitated* the conduct by the petitioner of an extensive educational campaign, the object of which was to acquaint and impress upon the American people and their representatives in Congress, the justice of the claims of the petitioner's principals. . . . The objective of the educational campaign so carried on by the petitioner *was accomplished* by the passage of the ‘Settlement of War Claims Act of 1928’.” (Italics added)

Despite that definite agreement of the parties, the opinion of Judge Biggs makes the statements that we neither proved the necessity nor showed the accomplishment as a “proximate cause”.

The case could have been presented to the Board by detailed evidence that would have required as many years for trial, as the work in obtaining the Act of Congress. But such had no necessity, by reason of the Stipulation of Facts. The issue before the Board was a very narrow issue. The majority opinions disregard the agreement of parties, create an entirely new issue, find our contracts and actions illegal *ipso facto*, and declare that even where the very business of the taxpayer is the obtaining of an Act of Congress, the expenses cannot be deducted but the receipts must be “taxed”.

To the ends of Justice, we submit, this Court should assume jurisdiction over such a situation.

10. The holding by the judges of the Third Circuit, that they may decide a case as a five-man circuit court of appeals, notwithstanding Judicial Code, Section 117, declaring:

“There shall be in each circuit a circuit court of appeals, which shall consist of three judges, of whom two shall constitute a quorum . . .” ,

is in conflict with the opposite views of the judges in the Ninth Circuit, *Lang's Estate v. Commissioner*, 97 Fed. (2d) 867, wherein that court certified questions to the Supreme Court (answered by this Court in 309 U. S. 264), because the judges of the Ninth Circuit deemed that they lacked authority to sit as a court by any greater number than the three judges prescribed by the Judicial Code, even though there stood in the Ninth Circuit a situation of conflicting decisions or views upon the same question of construction or application of the revenue-laws (which latter was not true in the case at bar).

Additionally, in at least three instances the Circuit Court of Appeals for the District of Columbia has denied the right to hearings by courts comprising all of the judges holding appointment to that circuit (with denial of Certiorari by this Court in two of the three instances); See, *United States, ex rel. v. Coe*, 302 U. S. 721, 776; 304 U. S. 589; *Davis v. Davis*, 305 U. S. 32; *Cox v. Thompson*, 305 U. S. 606.

The increases in the number of circuit judges in respective circuits repeatedly has occurred by Acts of Congress at the suggestion of the Attorney General, by reason of congested conditions in various circuits and resulting delays in trials, the available number of judges being insufficient to permit enough sittings of courts of three judges to handle the Calendars, and the addition of such new appointments permitting rotations of judges in sittings by three-judge courts. The intention of Congress for such a rotation, will be nullified by "courts en banc", wholly or partially, dependent upon the extent to which the practice may be carried. Furthermore, since by Judicial Code, Section 120, district judges may be assigned to comprise "the full court", if the term "full court" means a "court en banc" the work of the district courts may experience interference and congestion, if district judges are to be assigned to "courts en banc",—which, again, frustrates the intention of Congress in legislating for additional district judges.

The several opinions in the case at bar, illustrate the divergence of views by increase in number of judges beyond the prescribed three. Extension to the circuits where seven judges hold appointment, will increase the difficulty in ascertainment of a common ground for judicial decision.

The very length of this Petition has been necessitated by the difficulty in ascertaining just what was decided by "the court", and by *which* "court". Out of the five judges who heard this case, it is possible to find ten "circuit courts of appeals" in terms of three judges. The Rules of Third Circuit sanction a "court en banc".

The importance of the entire matter, for consideration by this Court, appears self-evident. Equally, that this Court should determine whether the Associate Justice assigned to a circuit, is an essential member of a "court en banc", if more than three judges is permissible,—or the Chief Justice or a District Judge of the Circuit.

11. The distinction made by the opinion of Judge Biggs, with which one other judge (Jones) agreed, but with which two other judges (Maris and Goodrich) disagreed, thus expressing an equal division of views within the Third Circuit, between "favor legislation" and "debt legislation", involves a basic and "an important question of federal law which has not been, but should be, settled by this court" (Rule 38, 5(b), Rules of this Court).

12. Rule 4 of the Third Circuit recognizes that two judges shall constitute a quorum, regardless of whether the "court" comprises three judges or sits "en banc". Accordingly, the views of Judge Maris as concurred in by Judge Goodrich, represents a quorum of a court "en banc" equally as well as a quorum of three judges. The Rules contain no provision for control by a majority, in a "court" exceeding the three judges prescribed by the Judicial Code. Accordingly, the opinions in the Third Circuit stand susceptible into expressions of conflicting views by *two* "courts en banc" within that same circuit, and further emphasizing

the importance of the matter as a reason for consideration by this Court.

Wherefore, it respectfully is submitted that this petition should be granted.

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APPENDIX.

Statutes and Regulations Involved.

Revenue Act of 1928, Section 23, Deductions From Gross Income.

In computing net income there shall be allowed as deductions:

(a) **EXPENSES.**—All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered; . . .

Regulations 74.

Article 121 (at page 34):

BUSINESS Expenses. Business expenses deductible from gross income include the ordinary and necessary expenditures directly connected with or pertaining to the taxpayer's trade or business, except the classes of items which are deductible under the provisions of articles 141-271. . . . Among the items included in business expenses are management expenses, commissions, labor, supplies, incidental repairs, operating expenses of automobiles used in the trade or business. . . . A taxpayer is entitled to deduct the necessary expenses paid in carrying on his business from his gross income from whatever source. As to items not deductible, see section 24 and articles 281-284.

Revenue Act of 1928, Section 23, Deductions From Gross Income.

In computing net income there shall be allowed as deductions:

. . . (n) **CHARITABLE AND OTHER CONTRIBUTIONS.**—In the case of an *individual*, contributions or gifts made within the taxable year to or for the use of. . . . (Italics added)

Regulations 74.

Article 261. *Contributions or gifts by individuals* (at page 85)

.....

Article 262. *Donations by corporations.* (at page 86)

Corporation are not entitled to deduct from gross income contributions or gifts which individuals may deduct under section 23(n). Donations made by a corporation for purposes connected with the operation of its business, however, when limited to charitable institutions, hospitals, or educational institutions conducted for the benefit of its employees or their dependants are a proper deduction as ordinary and necessary expenses. Donations which legitimately represent a consideration for a benefit flowing directly to the corporation as an incident of its business are allowable deductions from gross income. For example, a street railway corporation may donate a sum of money to an organization intending to hold a convention in the city in which it operates, with the reasonable expectation that the holding of such convention will augment its income through a greater number of people using the cars. Sums of money expended for lobbying purposes, the promotion or defeat of legislation, the exploitation of propaganda, including advertising other than trade advertising, and contributions for campaign expenses, are not deductible from gross income.

Judicial Code, Section 117. (U. S. Code Annotated, Sec. 212)

There shall be in each circuit a circuit court of appeals, which shall consist of three judges, of whom two shall constitute a quorum, which shall be a court of record, with appellate jurisdiction, as hereinafter limited and established.

Judicial Code, Section 118. (U. S. Code Annotated, Sec. 213)

... The circuit judges in each circuit shall be judges of the circuit court of appeals in that circuit, and it shall be the duty of each circuit judge in each circuit to sit as one of the judges of the circuit court of appeals in that circuit from time to time according to law. ...

Judicial Code, Section 120. (U. S. Code Annotated, Sec. 216)

The Chief Justice and the associate justices of the Supreme Court assigned to each circuit, and the several

district judges within each circuit, shall be competent to sit as judges of the circuit court of appeals within their respective circuits. . . . In case the full court at any time shall not be made up by the attendance of the Chief Justice or the associate justice, and the circuit judges, one or more district judges within the circuit shall sit in the court according to such order or provision among the district judges as either by general or particular assignments shall be designated by the court. . . .

Internal Revenue Code, Section. 1142.

Petition for Review. The decision of the Board . . . may be reviewed by a circuit court of appeals . . . as provided in section 1141.

Internal Revenue Code, Section 1140.

Date When Board Decision Becomes Final.

The decision of the Board shall become final—

(a) *Petition for Review Not Filed On Time.*— Upon the expiration of the time allowed for filing a petition for review, if no such petition has been fully filed within such time; or

(b) *Decision Affirmed or Petition for Review Dismissed*—

(1) *Petition for certiorari not filed on time.*—Upon the expiration of the time allowed for filing a petition for certiorari, if the decision of the Board has been affirmed or the petition for review dismissed by the Circuit Court of Appeals and no petition for certiorari has been duly filed; or

(2) *Petition for certiorari denied.*—Upon the denial of a petition for certiorari, if the decision of the Board has been affirmed or the petition for review dismissed by the Circuit Court of Appeals; or . . .

(e) *Definitions.*—As used in this section—

(1) *Circuit Court of Appeals.*—The term “Circuit Court of Appeals” includes the United States Court of Appeals for the District of Columbia. . . .

CHARLES E. YOUNG 2404

IN THE
Supreme Court of the United States

OCTOBER TERM, 1941.

No. 34

TEXTILE MILLS SECURITIES CORPORATION, *Petitioner*,

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent*.

On Writ of Certiorari to the Circuit Court of Appeals
for the Third Circuit.

BRIEF FOR THE PETITIONER.

✓ EDMUND S. KOCHERSPERGER,
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IN THE
Supreme Court of the United States

OCTOBER TERM, 1941.

No. 34

TEXTILE MILLS SECURITIES CORPORATION, *Petitioner*,

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent*.

On Writ of Certiorari to the Circuit Court of Appeals
for the Third Circuit.

BRIEF FOR THE PETITIONER.

OPINIONS BELOW.

The opinions of the court below (R. 42-75) are reported in 117 Fed. (2d) 62.

JURISDICTION.

A judgment of the court below was entered on December 7, 1940 (R. 75). A motion for judgment, filed by the petitioner, (R. 76-78) was denied on January 3, 1941 (R. 79). The petition for a Writ of Certiorari was filed on March 5, 1941 (R. 80). The petition for a Writ of Certiorari was granted March 31, 1941 (R. 80). The jurisdiction of this Court rests on Section 3(b) of the Act of February 13, 1925, as amended by the Act of May 22, 1939.

GENERAL QUESTION PRESENTED.

Whether, in the determination of taxable net income, the American corporate-agent for former enemy-aliens whose property had been seized under the Trading With the Enemy Act, is entitled to deduction for the expenses incurred by the agent in procuring an Act of Congress which accorded a partial recognition of the claims of the former enemies, where the agent's contracts for the services required the agent to bear all expenses and provided that the agent would receive compensation (including reimbursement for the expenses) upon the basis of a contingent fee percentage relative to the amounts recovered by the former enemies as the result of such Act of Congress.

SUBSIDIARY OR COLLATERAL QUESTIONS RESULT FROM COMMENTS BY OPINIONS IN THE COURT-BELOW.

1. Whether it was void or illegal for Americans to contract for the representation in the United States on behalf of former enemy-aliens in obtaining action by Congress for the recognition of claims by the aliens whose properties had been seized during the World War of 1914-1918 under the authority of the Trading with the Enemy Act, which Act specifically provided in part:

“after the end of the war any claim of any enemy or an ally of enemy to any money or other property received and held by the Alien Property Custodian or deposited in the United States Treasury, shall be settled as Congress shall direct.”;

either because such legislation was “favor legislation” as distinct from “debt legislation”, or because the contracts required compensation upon a contingent basis, or for any other reason.

2. If the contracts were void or illegal, whether the expenses incurred in an illegal business are deductible as “ordinary and necessary expenses” in the ascertainment of

taxable income, despite the illegality of the contracts and the business undertaking of representation of the claimants.

3. If the contracts were valid and if the business of the petitioner was legal, whether the deduction of the expenses as "ordinary and necessary expenses" is to be denied by reason of Article 262 of the Regulations 74 dealing specifically with the subject of "Donations by Corporations" and a reenactment of the provisions of the Revenue Act without change by Congress in the section of the Act according deduction for "ordinary and necessary expenses".

4. Whether a circuit court of appeals is authorized to sit and decide a case by a composition of judges comprising a greater number than the three judges prescribed by the Judicial Code, Section 117, and where different views have been expressed by several groups of judges within a total of judges exceeding the prescribed three-judges, which views shall prevail as the judgment of a circuit court of appeals.

5. If a circuit court of appeals is authorized to decide a case by a court *en banc* whose composition exceeds the three-judges prescribed by the Judicial Code, what is the proper composition of a court *en banc* in a Judicial Circuit under the Federal statutes, and is the Circuit Justice an essential member of such a court.

6. Where the Rules of the Third Judicial Circuit prescribe that two judges shall constitute a quorum when the judges sit as a court *en banc* and, in the case at bar, two such quorums have expressed contrary conclusions in the case, which views shall prevail as expressing a judgment of the court.

7. Whether a circuit court of appeals, by an enlargement into a court *en banc* of five judges, has the right by a majority of three judges to reverse a Board decision for reasons and upon issues which were not presented in the Board proceedings.

STATUTES AND REGULATIONS INVOLVED.

Revenue Act of 1928, Section 23, Deductions From Gross Income.

In computing net income there shall be allowed as deductions:

(a) **EXPENSES.**—All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered; * * *

Regulations 74.

Article 121 (at page 34):

BUSINESS Expenses. Business expenses deductible from gross income include the ordinary and necessary expenditures directly connected with or pertaining to the taxpayer's trade or business, except the classes of items which are deductible under the provisions of articles 141-271. * * * Among the items included in business expenses are management expenses, commissions, labor, supplies, incidental repairs, operating expenses of automobiles used in the trade or business. * * * A taxpayer is entitled to deduct the necessary expenses paid in carrying on his business from his gross income from whatever source. As to items not deductible, see section 24 and articles 281-284.

Revenue Act of 1928, Section 23, Deductions From Gross Income.

In computing net income there shall be allowed as deductions:

* * * (n) **CHARITABLE AND OTHER CONTRIBUTIONS.**—In the case of an *individual*, contributions or gifts made within the taxable year to or for the use of. * * * (Italics added)

Regulations 74.

Article 261. *Contributions or gifts by individuals* (at page 35)

.....

Article 262. *Donations by corporations.* (at page 86)

Corporations are not entitled to deduct from gross income contributions or gifts which individuals may deduct under section 23(n). Donations made by a corporation for purposes connected with the operation of its business, however, when limited to charitable institutions, hospitals, or educational institutions conducted for the benefit of its employees or their dependants are a proper deduction as ordinary and necessary expenses. Donations which legitimately represent a consideration for a benefit flowing directly to the corporation as an incident of its business are allowable deductions from gross income. For example, a street railway corporation may donate a sum of money to an organization intending to hold a convention in the city in which it operates, with the reasonable expectation that the holding of such convention will augment its income through a greater number of people using the cars. Sums of money expended for lobbying purposes, the promotion or defeat of legislation, the exploitation of propaganda, including advertising other than trade advertising, and contributions for campaign expenses, are not deductible from gross income.

Judicial Code Section 117. (U. S. Code Annotated, Title 28, Sec. 212)

There shall be in each circuit a circuit court of appeals which shall consist of three judges, of whom two shall constitute a quorum, which shall be a court of record, with appellate jurisdiction, as hereinafter limited and established.

Judicial Code, Section 118. (U. S. Code Annotated, Title 28, Sec. 213)

* * * The circuit judges in each circuit shall be judges of the circuit court of appeals in that circuit, and it

shall be the duty of each circuit judge in each circuit to sit as one of the judges of the circuit court of appeals in that circuit from time to time according to law. * * *

Judicial Code, Section 120. (U. S. Code Annotated, Title 28, Sec. 216)

The Chief Justice and the associate justices of the Supreme Court assigned to each circuit, and the several district judges within each circuit, shall be competent to sit as judges of the circuit court of appeals within their respective circuits. * * * In case the full court at any time shall not be made up by the attendance of the Chief Justice or the associate justice, and the circuit judges, one or more district judges within the circuit shall sit in the court according to such order or provision among the district judges as either by general or particular assignments shall be designated by the court. * * *

STATEMENT.

1. Facts Regarding the Merits of the Case.

The petitioner was obligated by contracts (R. 29-34) to represent in the United States foreign claimants comprising former enemy-aliens whose properties had been seized under the authority of the Trading with the Enemy Act of 1917,

“to protect the interest of the Claimant in moneys and or securities or properties now held in trust for the Claimant by the Alien Property Custodian, and to bring about the return of the Claimant's property” * * * (R. 33)

The contracts were entered into in Germany in the individual name of the president of the petitioner corporation and later were assigned to the company. (R. 34)

The contracts required “the Agent * * * to meet all costs and expenses incurred in the performance of his agency”. (R. 33)

The compensation to the Agent was fixed at a percentage basis relative to the amount of recovery by the claimants

(R. 33), 3 per cent upon the amount received by the claimant at any time and an additional 2 per cent upon "the amounts actually paid to the Claimant within one year after enactment of such legislation". (R. 33)

It was agreed by both litigants in the Board proceedings by a Stipulation of Facts (R. 30-31; 34-36);

"The obligations of the petitioner under the afore-said representation contracts were such as *necessitated* the conduct by the petitioner of an extensive educational campaign, the object of which was to acquaint and impress upon the American people and their representatives in Congress, the justice of the claims of the petitioner's principals. Such a campaign was conducted by the petitioner at its own expense. The carrying on of this campaign involved the gathering and dissemination of historical data and precedents in respect of the policy of the United States relative to enemy-owned properties within its borders in times of war, international relations, treaty rights, etc., as well as the preparation and making of appropriate proposals and suggestions to Members of Congress, with the view to the expeditious enactment of the sought-for legislation. For these purposes the petitioner engaged the services of various persons and organizations, including Ivy Lee, W. F. Martin, J. Reuben Clark, . . . The services of the "Ivy Lee" organization were utilized in connection with matters of publicity; including the making of arrangements for speeches and speakers around the country, cooperating with the Press in editorial comments, as well as news items, and work of a general publicity nature. The services of W. F. Martin and J. Reuben Clark were utilized in connection with the preparation of propaganda concerning international relations, treaty rights, and the historical policy of the United States relative to enemy-owned property in times of war. Their views on these subjects were expressed in several publications; one during the year 1926, which was presented to the Senate by a Member of that Body, entitled "American Policy Relative to Alien Enemy Property," which was published as Senate Document No. 181, Sixty-ninth Congress, Second Session, a true and correct copy of which is attached hereto and made a part hereof as Ex-

hibit "B"; another, entitled "Status of Ex-enemy Property, Interpretation of Treaties and Constitution," being a forty-three page pamphlet, which was widely distributed through the facilities of "Ivy Lee," and otherwise, a true and correct copy of which is attached hereto and made a part hereof, as Exhibit "C," . . . Messrs. Lee, Martin, Clark . . . continued their respective services, as hereinabove described, to the petitioner until the enactment of the "Settlement of War Claims Act of 1928," on March 10, 1928 . . . The objective of the educational campaign so carried on by the petitioner was accomplished by the passage of the "Settlement of War Claims Act of 1928," supra, subsequent to which no services were rendered to the petitioner by Messrs. Lee, Martin, and Clark." (Italics added.)

In its Opinion, the Board stated (R. 14):

" . . . the stipulation is adopted as our findings herein. We shall set forth so much of the facts as is considered necessary for discussion of the issue to be determined."

The Board also stated (R. 18):

"He (*the Commissioner*) makes no claim that the acceptance of employment such as is involved in this proceeding was not within the scope of petitioner's powers or business. Neither does he make any claim that the expenses incurred were not in fact ordinary and necessary in performing the services required of it under its contracts." (*Italicized explanation added.*)

The Board concluded (R. 21, 22):

"The respondent has made no claim, as we have pointed out, that such employment was outside the scope of petitioner's powers or business and we have concluded from the record that the services rendered were necessary for the accomplishment of the desired result. There has been no showing that the petitioner indulged in any questionable practices in carrying out the purposes of its employment and no showing or claim that the activities in respect of which the ex-

penses were incurred were against public policy . . . Accordingly we are unable to reach any conclusion except that the expenses here in question were in fact 'ordinary and necessary' in the conduct of petitioner's business and, having reached that conclusion, it is our opinion that the statute directs their allowance as deductions in determining petitioner's net income . . ."

The opinion of Judge Maris (R. 66-75) concurred in by Judge Goodrich, agreed with the Board.

So far as a unity of views can be found in the two opinions of the three other judges who held against the petitioner in the court below, the facts found by the Board were disregarded and the conclusion for reversal of the Board decision was reached by injecting into the case issues that neither were argued nor were even suggested in the Board proceeding, and which definitely were excluded from the Board proceedings by a Stipulation of Facts and the Commissioner's actions through his legal representatives.

2. Facts Regarding Procedure.

The litigation was initiated by Notice of Deficiency (R. 2-11) from the Commissioner and the statement therein (R. 11):

"The amounts of \$96,000.¹ and \$47,500. representing sums spent for the promotion of legislation are not deductible from gross income in accordance with article 262 of Regulations 74 promulgated under the Revenue Act of 1928 and section 43² of the same Act."

The Commissioner's determination was reviewed by the Board of Tax Appeals, the evidence comprising the Petition so far as admitted by Answer and a Stipulation of Facts (R. 29-38). The decision of the Board held that there

¹ By Stipulation (R. 35, 36) the Commissioner later admitted that \$51,000 of that \$96,000 was allowable as deduction.

² Reference to section 43 later became inapplicable because the Commissioner conceded that the items of \$45,000 and \$47,500 were properly accrued. (R. 38.)

was no deficiency (R. 23), because the expenses were deductible as ordinary and necessary expenses. The opinion of the Board is found in R. 13-22, and in 38 B. T. A. 623.

The Commissioner filed a Petition for Review (R. 23-27) with the Circuit Court of Appeals for the Third Circuit, on February 13, 1939 (R. 23).

Effective March 1, 1940, the judges of the Third Circuit amended the Rules of that Circuit (R. 74). Rules 4 and 5 made provision for consideration and hearings by "the court en banc" (R. 50, 51).

After an original argument before a court of three judges (R. 41), the reargument of this case was ordered "before the court en banc" (R. 41). That argument occurred July 1, 1940, before the five circuit judges of the Third Judicial Circuit, Biggs, Maris, Clark, Jones, and Goodrich (R. 42).

Three opinions were rendered December 7, 1940; one by Judge Biggs concurred in by Judge Jones (R. 42-58), a separate opinion by Judge Clark (R. 58-66), and one by Judge Maris concurred in by Judge Goodrich (R. 66-75).

A judgment bears date December 7, 1940, over the signature of John Biggs, Jr., Circuit Judge (R. 75) ordering:

"that the decision of the said Board of Tax Appeals in this cause be, and the same is hereby reversed, and the cause is remanded to the said Board of Tax Appeals with the direction to redetermine the tax in accordance with the view expressed by the majority of this court."

On December 27, 1940, the respondent below (the petitioner herein) filed a Motion for Judgment, addressed to a circuit court of appeals comprising Judges Maris and Goodrich as a quorum of two judges in a circuit court of appeals as prescribed by Section 117³ of the Judicial Code (R. 76-78). That Motion was denied January 3, 1941 (R. 79).

³ Judicial Code, Section 117. "There shall be in each circuit a circuit court of appeals, which shall consist of three judges, of whom two shall constitute a quorum. . ."

SPECIFICATION OF ERRORS URGED.

1. A circuit court of appeals comprising Judges Maris and Goodrich as a quorum of two judges in a court of three judges specified by Judicial Code, Section 117, erred in refusing to order an entry of judgment of affirmance of the Board decision, as demanded by petitioner's Motion for Judgment.

2. The judgment of reversal of the Board decision is invalid because rendered as the action by a majority of five judges, instead of by a court of three judges as specifically provided by the Judicial Code, Section 117 and by the other pertinent provisions of that Code.

3. The alleged court en banc was illegally constituted, since it did not include within its membership the Associate Justice who was assigned as a Circuit Justice to the Third Judicial Circuit, nor the Chief Justice, nor a District Judge of the Circuit.

4. The circuit judges of the Third Judicial Circuit erred in holding and deciding that those judges, to the exclusion of the Circuit Justice holding assignment to that judicial circuit, the Chief Justice or a District Judge, can sit and decide a case as a "court en banc" in a situation (such as in the case at bar) where decisions within that circuit do not stand in a state of conflict and where the decision in the specific case would not stand in conflict with any prior decision within that circuit.

5. The Rule 4 of the Third Judicial Circuit, by authority of which the five judges purported to decide the case at bar by a majority of three judges to two judges, violates Article III, Section 1, of the Constitution of the United States, for the reason that a five-men court is not a part of "such inferior Courts as the Congress may from time to time ordain and establish", and to the contrary the Congress has prescribed a circuit court of appeals as a three-men court.

6. Any set up of five judges into a validly constituted circuit court of appeals of three members wherein any two of Judges Biggs, Clark, and Jones comprised a quorum of two judges, erred in holding and deciding that, collectively or alternatively:

(a) Petitioner's contracts were invalid or void as being against public policy.

(b) The facts as agreed upon between the parties and as found to be the facts by the Board, can be disregarded as the facts, and an adverse decision be rendered upon a different assumption of the facts, as made by such a quorum of judges.

(c) Petitioner's contracts or services sought the enactment of "favor legislation", as distinct from "debt legislation".

(d) The Trading With The Enemy Act did not in itself create "debt legislation".

(e) The Settlement of War Claims Act of 1928 was not in settlement of claims that Congress recognized to be existent by the expressed provisions of the Trading With The Enemy Act.

(f) The petitioner's expenses were not ordinary and necessary expenses within the construction of the Revenue Act of 1928.

(g) There is a conclusive and un rebuttable presumption of law that every contract requiring the performance of services for the procurement of "favor legislation" is improper, inferentially fraudulent or wrongful, and basically void as being against public policy, regardless of the contrary statement by the Board that no such issue was presented in the case before the Board.

(h) The opinion of Judge Maris, concurred in by Judge Goodrich, did not express the correct legal principles as the basis for a judgment affirming the Board decision.

(i) The circuit court of appeals can depart from the accepted and usual course of judicial proceedings, by reversing the Board on an issue that was not raised in the Board and wherein the advancing of the issue by the respondent for the first time within a circuit court of appeals represents a shift to a ground which the taxpayer had every reason to think was abandoned in the earlier stage of the litigation when before the Board.

(j) The cause should be remanded to the Board with the direction to redetermine the tax in accordance with the view expressed by the majority, and without according the petitioner any opportunity for the presentation of additional evidence material to the new issue first raised by the court itself in the opinions of Judges Biggs and Clark.

(k) That Congress, by the reenactment of the revenue-laws without change in the language for deduction of "ordinary and necessary expenses", is to be presumed as having approved Article 562 of Regulations 69 (dealing with the subject "Donations by Corporations"), just as if that Article had been incorporated into Article 101 (which dealt specifically with "ordinary and necessary expenses"), although neither Article made the slightest specific reference to the other Article, and further, that Congress is to be presumed by such reenactment to have given its approval to an interpretation which the Bureau, for the first time, makes *in the very case at bar*.

(l) The ordering of a judgment of reversal of the decision of the Board of Tax Appeals.

7. If the court of five judges constitutes a validly composed circuit court of appeals for the Third Circuit, the court erred in holding and deciding relative to all of the grounds set forth herein under subdivision 6, (a) to (l) inclusive.

8. Although no statute or law enacted by Congress prohibited any of the actions engaged in by the petitioner in

performance of its contract obligations, the holding by Judges Biggs, Jones and Clark, converts without authority of law, the revenue-laws into a penal statute imposing a fine levied upon the petitioner's gross receipts because the petitioner engaged in a valid, legal, and unprohibited business undertaking which those judges personally did not favor, the holding in that regard constituting unconstitutional judicial legislation as an unauthorized assumption of the powers conferred by the Constitution upon the Congress.

SUMMARY OF THE ARGUMENT.

The petitioner was engaged in the business of representing foreign principals in obtaining the restoration by an Act of Congress, of property seized under the Trading with the Enemy Act. The expenses in question were sustained in that business. The business was legitimate and proper. The undertaking was legal. Nothing unconscionable or improper was done. The disallowance of deduction as "ordinary and necessary expenses" finds no justification from the mere fact that the business involved the procurement of an Act of Congress under the peculiar facts of this most exceptional case, including the necessity for contingent compensation.

The legal conclusions expressed by the Board (R. 17-22) and by a quorum of two judges (Maris and Goodrich) in the Circuit Court of Appeals for the Third Judicial Circuit (R. 66-75), merit the approval by this Honorable Court through the appropriate judgment in favor of the petitioner or, if additional evidence is deemed essential to the ends of Justice, the proceeding should be remanded to the Board for a rehearing.



ARGUMENT.**Part 1. The Issue Before the Board.****I.**

A majority of three judges in the court-en-banc, affirmed the board on the only issue presented to the board, but a different majority of three judges reversed the board upon issues which were not presented to the board.

Prejudice to the petitioner by the consideration of the case by a court *en banc*, instead of by the three judges specified in the Judicial Code, comes not from a court *en banc* as such, but from the fact that three out of the five judges saw fit to join in an adverse decision upon issues that were not presented in the Board proceedings and by a disregard of the facts as found by the Board.

The three opinions in the court-below show, that one of those three adverse-judges (Judge Clark) actually agreed with the two dissenting-judges relative to the single issue that was presented to and was decided by the Board, thus evidencing that if the court *en banc* properly had confined its consideration to a review of the issue that was presented to the Board, the judgment would have affirmed the Board decision.

In that event, the Government would have borne the burden of a petition for certiorari and, when granted, the same single issue would stand for consideration by this Court as was decided by the Board.

As matters now stand, however, this petitioner is obliged to maintain the burden and to argue issues additional to that in the Board proceeding.

The issue before the Board was clearly defined.

By Section 23(a) of the Revenue Act of 1928, Congress accorded a deduction from the gross receipts in the ascertainment of taxable net income, for:

"All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, *including a reasonable allowance for salaries or other compensation for personal services actually rendered.*" (Italics added)

The items in dispute in this case constituted "other compensation for personal services actually rendered," and were of no other nature as "ordinary and necessary expenses." The reasonableness of the amounts never were questioned by the Commissioner throughout the controversy, nor did he ever contend that the personal services were not actually rendered. As the italicized words are explanatory of "ordinary and necessary expenses," definitely expressing the thought that "compensation for personal services actually rendered" is "ordinary and necessary expenses" to the extent of reasonableness in amounts, a failure by the Commissioner to question either the amounts or the rendition of the services, would appear necessarily to admit the expense as being of the nature "ordinary and necessary."

When the case was heard by the Board the issue was a simple one. It finds statement in the Commissioner's notice of deficiency (R. 11): .

"The amounts of (\$45,000.)¹ and \$47,500, representing sums spent for the promotion of legislation are not deductible from gross income in accordance with Article 262 of Regulations 74 promulgated under the Revenue Act of 1928"²

In addition to the fact that the Commissioner never questioned in the Board proceedings the reasonableness of the amounts, the rendition of the services, or the nature of the expenses as being incurred as "ordinary and necessary

¹ Reduced from \$96,000 stated in the notice, by the Commissioner's admission in the Stipulation of Facts.

² Language omitted, also covered by the Stipulation of Facts.

expenses" in carrying on the taxpayer's business, the Commissioner agreed with us by the Stipulation of Facts:

"The obligations of the petitioner under the afore-said representation contracts were such as *necessitated* the conduct by the petitioner of an extensive educational campaign, the object of which was to acquaint and impress upon the American people and their representatives in Congress, the justice of the claims of the petitioner's principals." (R. 30.) (Italics added.)

Parenthetically, we direct attention to that word "necessitated," in view of statement in the opinion of Judge Biggs that we "failed to prove" that the services were "necessary." The facts as agreed-to, must have escaped the Judge's attention. We continue quotation from the Stipulation:

"Such a campaign was conducted by the petitioner at its own expense. The carrying on of this campaign involved the gathering and dissemination of historical data and precedents in respect of the policy of the United States relative to enemy-owned properties within its borders in times of war, international relations, treaty rights, etc., as well as the preparation and making of appropriate proposals and suggestions to Members of Congress, with a view to the expeditious enactment of the sought-for legislation." (R. 30, 31)

"For these purposes the petitioner engaged the services of various persons and organizations . . ." (R. 31) —(the Stipulation naming the three persons related to the items in dispute).

"The objective of the educational campaign so carried on by the petitioner was accomplished by the passage of the "Settlement of War Claims Act of 1928" . . ." (R. 34)

Again parenthetically,—yet, says the opinion of Judge Biggs, we failed also to prove a proximate causation between the services and the legislation. The Stipulation ap-

pears to have been overlooked in every respect. We resume quotation from the Stipulation:

"The parties hereto agree that these . . . obligations so incurred . . . represent expenses incurred by the petitioner directly in connection with the campaign carried on by it, as aforesaid, the purpose of which was accomplished by the enactment by Congress of the 'Settlement of War Claims Act of 1928,' as aforesaid." (R.36)

Truly, and correctly, we did not include in the Stipulation the entire history of the Trading with the Enemy Act, nor of the several Acts which accorded gradual restitutions to the enemies, nor of the Settlement of War Claims Act which related to the properties that then remained; nor did we go into extensive detail by agreeing that the American-claimants against Germany were seeking satisfaction for *their* claims by urging upon Congress the confiscation of the properties that had been seized from the enemies and still remained, and that their propaganda for confiscation had to be met by honest and true statements on our part in protection of our principals' rights or claims; nor did we explain why the contingent-contracts were the only way that the thing could be handled.

The Stipulation covered *the issue that was before the Board*, and was confined to the facts that were essential for the understanding of that issue.

The Board found the facts as stated in the Stipulation (R. 14).

The sole and only issue before the Board related to the single question whether the Article 262 of Regulations 74 precluded the deduction of these expenses that were admittedly "ordinary and necessary expenses."

The Board so stated the matter in the Opinion (R. 17, 18):

"In his notice of deficiency the respondent rested his disallowance of the deductions here in issue on the provisions of article 262 of Regulations 74, which states

in part that 'Sums of money expended for lobbying purposes, the promotion or defeat of legislation, the exploitation of propaganda, including advertising other than trade advertising, and contributions for campaign expenses, are not deductible from gross income.' He makes no claim that the acceptance of employment such as is involved in this proceeding was not within the scope of petitioner's powers or business. *Neither does he make any claim that the expenses incurred were not in fact ordinary and necessary in performing the services required of it under its contract.* He now rests his claim wholly upon the decision of the United States Circuit Court of Appeals for the Ninth Circuit in *Sunset Scavenger Co. v. Commissioner*, 84 Fed. (2d) 453, which reversed the Board and approved the regulation cited. At the hearing his counsel stated that 'the question in one sentence is whether the Board will follow that decision or whether it won't.' (Italics of opinion, added).

Before the Board the question was "in one sentence,"—relating wholly to the Article in the Regulations. When the case gets through a court *en banc*, the "one sentence" has carried into the whole field of jurisprudence, ethics, morality, crime, public policy,—even to the extent of interpreting the congressional-intent of the 1928-Congress by the presumed intentions of a different Congress of 1936, or *eight years* after the event.

When a case is presented to the Board upon such a narrow and clear-cut issue, it hardly can be expected that either party will encumber the record by a lot of extraneous material that holds no relation to that issue.

So far as the Commissioner was concerned, he was relying wholly upon the Article 262 and it made no difference what was done or how it was done. So far as he was concerned, our motives and actions could be beyond reproach or criticism; the expenses could be "ordinary and necessary expenses" and still be non-deductible because of the Article 262. *We were seeking legislation*, and that Article 262 stood as "the supreme law of the land," to deny the

deduction of our expenses. That, was the Commissioner's position before the Board. For our part, we contended that the Article did not apply to the facts of our situation anyway; further, that the Commissioner's interpretation of the Article was incorrect; we distinguished our situation from the *Sunset Scavenger* case (*supra*) and contended that, if applicable to our situation, the decision was bad law.

Of course, we were "seeking legislation." That was our very business, the thing for which we had been engaged. We had not the slightest desire for any concealment. If our commissions (which included reimbursement for our expenses) were income, we had no element of gain or profit except as our receipts exceeded the expenses.

The Board rendered its decision in our favor, holding that the Article 262 did not bar the deductions, closing the Opinion as follows:

"The respondent has made no claim, as we have pointed out, that such employment was outside the scope of petitioner's powers or business and we have concluded from the record that the services rendered were necessary for the accomplishment of the desired result. There has been no showing that the petitioner indulged in any questionable practices in carrying out the purposes of its employment and no showing or claim that the activities in respect of which the expenses were incurred were against public policy . . . Accordingly we are unable to reach any conclusion except that the expenses here in question were in fact 'ordinary and necessary' in the conduct of petitioner's business and, having reached that conclusion, it is our opinion that the statute directs their allowance as deductions in determining petitioner's net income . . ." (R. 21, 22)

That the sole issue related to the Article 262 further finds a confirmation in the dissenting opinion of three of the members of the Board (R. 22). It was their view that Article 262 controlled the matter, and their entire opinion relates to the Article 262.

If the Commissioner believed that anything was lacking in the record before the Board or in the statements by the

Board opinion, he could have filed a motion for rehearing. He did not do so (R. 1, 2). Instead, he carried the case upon the Board-record, by a petition for review to the Third Circuit. If the Commissioner had seen fit to raise new issues at a rehearing (as Judges Biggs and Clark did in their opinions), the taxpayer stood fully prepared to meet any and all such new issues.

The element that appears particularly to have disturbed those two judges was the fact that the contracts were contingent. There was an entirely valid reason for the contingent-fee arrangement. The devaluation of the German-Mark had destroyed most values in Germany, inasmuch that the claimants possessed no resources out of which to pay for our services, except the property in control of the Alien Property Custodian. Similar properties seized in England, France, and Italy, suffered confiscation by the terms of the Treaty of Versailles. Restrictions by laws in Germany precluded the transfer of money out of Germany, even if the claimants had possessed resources in their native country. For the same reasons, we had to advance the expenses for them, looking for our reimbursement of those expenses by a higher rate of contingent-fee, than if the circumstances had permitted direct payment of the expenses by the Germans themselves.

The very same thing that caused the American-claimants to seek from Congress the confiscation of the properties of German-nationals that stood in possession of the Alien Property Custodian, in satisfaction of their claims, was the cause of our contingent contracts,—namely, the financial collapse of Germany. That collapse prevented the payment of reparations by Germany and the performance of other obligations under the Treaty of Versailles and the Treaty of Berlin, including payment of the claims of Americans whose properties had been seized in Germany and who had suffered losses by the sinking of the *Lusitania* and otherwise.

The Settlement of War Claims Act of 1928 solved the problem relative to claims of Americans and Germans alike, without confiscation and by way of compromise between the respective claimants. We will cover that matter later in this brief. (Pages 53 to 76 herein)

Yet, without the slightest basis for the statements, and with a wholly silent Record in that regard, the two adverse opinions in the Third Circuit pin upon us "a sinister element" (R. 60) and an *ipso facto* illegality (R. 45), in the fact that the circumstances compelled our engagement by a contingent-fee contract arrangement,—without, moreover, according us the slightest chance for explaining "why." The situation held its own peculiar facts and, much as we might have preferred it, no different kind of arrangement was possible.

Even solvent clients sometimes insist upon contingent-fee contracts with their attorneys. Relative to the claimants whom we represented, there was no other choice, and whoever might represent them had to do so by that form of contract alone.

With reference to the single issue presented to the Board, the three opinions in the Third Circuit evidence that Judges Clark (R. 64, 65), Maris and Goodrich (R. 72-75), constitute a majority of a court *en banc* (unanimous as a court of three judges) in agreeing with the Board that the Article 262 does not preclude the deduction of the expenses in question, while a minority of two judges (Biggs and Jones) agreed with the dissenting members of the Board (R. 48, 49, 50).

Thus, it may be observed, that if the original court of three judges (Biggs, Clark, and Maris) had confined the issue to the only question presented to and decided by the Board, the decision would have affirmed the Board in favor of the taxpayer by a quorum comprising Judges Clark and Maris. However, by invoking the addition of two judges into the court and a resort to new issues which never were presented to the Board, we find the confusing result of the

three opinions and an adverse majority relative to those new issues.

We contemplate with juridical anxiety the chaos to Justice, if courts *en banc* are approved for circuits comprising six and seven judges, with majority decisions rendered relative to issues that were not presented in the trial courts.

But the judgment of reversal by the majority of the three judges in the court below, stands upon those extraneous issues and, by necessity, we must meet them because we deem the entire record as being before this Court by the granting of the Writ of Certiorari.

With all fairness to the judges of the Third Circuit, we state that the new issues were initiated into the case by the Commissioner's attorney in the appellate proceedings, an attorney who held no connection with the matter when it stood within the Board's jurisdiction.

We noted our objection to that procedure through our brief, by insisting that the argument should be confined to the issue which the Board decided, and we did not argue those new issues in the appellate court. By a statement in our brief, that statement being preliminary to our Argument and separately marked by a heading, we stated in part:

"The injection of this 'new issue,' we believe, results from the fact that the individuals who have prepared the brief on this appeal by the Commissioner, are entirely different persons from those who actually participated in the Board proceedings *and who knew what was the issue before the Board.*

That a new question which was not raised before the Board, cannot be injected for the first time upon an appeal, would appear to have been decided conclusively:

General Utilities & Operating Co. v. Helvering, 296 U. S. 200.

Helvering v. Savage, 297 U. S. 106.

Kottelman v. Commissioner, 81 Fed. (2d) 621.

- Botchford v. Commissioner*, 81 Fed. (2d) 914.
Helvering v. Montana Life Insurance Co., 84 Fed. (2d) 623.
Sabatini v. Commissioner, 98 Fed. (2d) 753.
Bagnall v. Commissioner, 96 Fed. (2d) 956.
Covington v. Commissioner, 103 Fed. (2d) 201.

Regardless of that well-settled principle, this Court readily will observe, that the expenses incurred in *procuring* an Act of Congress under a contract that required the services of procuring such an Act and which stated in effect that the expected commissions must reimburse for the expenses which the agent incurred, essentially must bear the characterization of being "ordinary"—according to every definition of that word.

Beyond the foregoing statement, we perceive no necessity for our further discussion of that phase of the brief on behalf of the Commissioner."

For the most recent discussion of the subject-matter of "new issues," with a possible application to the case at bar, we refer this Honorable Court to its opinion in *Hormel v. Helvering*, 312 U. S. 552.

We desire to make our position clear. The Record in the Board and transferred to the Circuit Court, was clear, by the Stipulation, the Board opinion, and the Commissioner's acceptance of the Board's statements by a failure to file motion for a rehearing. If the Commissioner desired to change the issue in the case, that should have been done in the Board proceedings. But, delaying until the appeal brought a record into the appellate court that contained none of the detailed evidence that would have been presented in the Board, except for the Commissioner's agreement by Stipulation and acceptance of the Board's statements by failure to move for a rehearing, constituted a trial *de novo* in the appellate court in the absence of an adequate record.

The Stipulation was the result by way of an agreement after many oral conferences with the Commissioner's at

torney. In those conferences "the cards were laid on the table face up", and only the single question regarding Article 262 was the Commissioner's choice as the matter to be reviewed by the Board. The Board states in its opinion that attorney's statement at the oral argument:

"the question in one sentence is whether the Board will follow that decision or whether it won't." (R. 18)

About *four years' time* was required from the start to the finish in the enactment of the Settlement of War Claims Act. Detailed evidence regarding what we did and the reasons therefore, would have necessitated a day-by-day account of what we did and of what many other persons did as the cause for our actions. Several hearings were held in the House and the Senate. Many bills were introduced. The history of everything that happened in Congress would have been required. All of that was unnecessary in the Board because the Commissioner confined the question to a single issue. Obviously, what was *not required* in the Board, did not stand in the Record before the Third Circuit.

We refused to argue those "new issues" in the Third Circuit, solely because the record before that court established an entirely different issue,—namely, the issue which was presented to the Board.

Three judges agreed with us and with the Board regarding the only issue that properly stood before the Third Circuit. Three judges agreed against us regarding the "new issues" that had not been presented to the Board. One judge (Judge Clark) constituted the third judge in the instance of each of the two majorities as a court *en banc*.

We deem that the main question before this Court is the same question as was decided by the Board, affirmed by three judges in the court-below,—namely, whether Article 262 bars the deduction of the expenses in question.

II.

Article 262 of Regulations 74 does not apply to the facts of this case.

A.—Analysis and Comments Regarding Commissioner's Contention.

The Commissioner contended in the Board and the Third Circuit, that "the reenactment rule" barred the deduction, and he relies upon Article 262 of Regulations 74.

The petitioner answers that contention;

1. The Commissioner's *true* contention is not for the application of "the reenactment rule", but for a *present construction* of the Article 262 which it is unreasonable to presume as being within the knowledge of Congress when enacting the Revenue Act of 1928.
2. The Commissioner's attempt to extend "the reenactment rule" to the facts of this case, merits a reconsideration of that rule and its repudiation by this Honorable Court.
3. The Article 262, in any sense of an approval by Congress, has reference to gifts or donations, and not to the kinds of business expenses involved in the case at bar.

Article 262 in Regulations 74, is in the same language as Article 562 of Regulations 69; the latter applied to the Revenue Act of 1926 and the former to the Revenue Act of 1928. The language of deduction for "ordinary and necessary expenses" was repeated in the 1928-Act similarly as in the 1926-Act. Relative to the 1926-Act, the Treasury gave an interpretation of "ordinary and necessary expenses" by Articles 101 to 112 of Regulations 69, and the Article 562 dealt with the subject of corporate *Donations*; relative to the 1928-Act, the Treasury gave an interpretation of "ordinary and necessary expenses" by Articles 121 to 132 of Regulations 74 (thus specifically construing Sec-

tion 23(a) of the 1928-Act, and quoting that subdivision (a) as a heading that preceded the Articles 121 to 132); fifty-one pages further-over in Regulations 74, the Treasury specifically interprets subdivision (n) of Section 23 of the 1928-Act, dealing with the subject "Charitable and other contributions", and covers the matter of interpretation by Article 261 as "Contributions or gifts by individuals" and by Article 262 as "Donations by corporations".

Now, declares the Commissioner,—when the 70th Congress repeated in the Revenue Act of 1928 the language of deduction for "ordinary and necessary expenses" similarly as was stated in the Revenue Act of 1926, the 435 Representatives and the 96 Senators and the President should have known that, when the Regulations covered "Donations" by corporations the Treasury meant "ordinary and necessary expenses" that were *not gifts or donations*,—even though in no place in the Regulations (74 or preceding) can there be found any interpretation of "ordinary and necessary expenses" in terms of denying deductions to individuals, partnerships, and trusts that were engaged in business, for expenses involving the "promotion or defeat of legislation", either as expenses *or donations*.

On behalf of the petitioner we assert, that those members of the 70th Congress are to be imputed with *no less* knowledge of the Regulations 69 (when repeating language in the 1928-Act), than the Treasury itself demonstrated when it compiled and promulgated the Regulations 74 as being applicable to the legislation which that 70th Congress so innocently had enacted.

The Article 121 of Regulations 74 bears the specific heading "Business expenses"; there is no cross-reference to Article 262; in fact, Article 121 closes with the statement,— "As to items not deductible, see section 24 and articles 281-284." Similarly, Article 561 of Regulations 69 dealt with corporate deductions, stating;

"In general the deductions from gross income allowed corporations are the same as allowed individuals, ex-

cept that corporations may deduct dividends as provided in paragraph (6) of section 234 (a) and *may not deduct contributions or gifts*. Particularly, as to business expenses, see articles 101-112 . . ." (Italics added)

Then follows in Regulations 69 the Article 562 on the stated subject of "Donations", opening with the statement:

"Corporations are not entitled to deduct from gross income contributions or gifts which individuals may deduct under paragraph (10) of section 214 (a)."

Following that statement in Article 562, are three sentences, each dealing with specific kinds of corporate-donations which are considered deductible because they are treated as "business expenses".

We quote those sentences:

"*Donations* made by a corporation for purposes connected with the operation of its business, however, when limited to charitable institutions, hospitals, or educational institutions conducted for the benefit of its employees or their dependents are a proper deduction as ordinary and necessary expenses."

"*Donations* which legitimately represent a consideration for a benefit flowing directly to the corporation as an incident of its business are allowable deductions from gross income.

"For example, a street railway corporation may *donate* a sum of money to an organization intending to hold a convention in the city in which it operates, with the reasonable expectation that the holding of such convention will augment its income through a greater number of people using the cars." (Italics above, added)

Then follows in Article 562 the sentence which causes this case:

"Sums of money expended for lobbying purposes, the promotion or defeat of legislation, the exploitation of propaganda, including advertising other than trade advertising, and contributions for campaign expenses, are not deductible from gross income."

We respectfully request consideration of the matter from the view-point of "knowledge by the 70th Congress". Nowhere in any of the revenue acts (then or preceding) was a corporation granted a deduction for "Charitable and other contributions". If the Members of Congress knew *anything*, they knew *that*. With no deduction granted by the Acts, there was no occasion that they read Regulations to ascertain an administrative interpretation regarding something *that was not in the Acts*. Properly, they might read the Article which dealt with "Business expenses", if they desired to know the administrative interpretation of "ordinary and necessary expenses". But, if they read the Article 101 (which stood at page 39 of Regulations 69) that related to "ordinary and necessary expenses", they would find no mention of *business expenses* connected with "the promotion or defeat of legislation",—still less, would they find any reference in Article 101 to the Article 562 (which stood at page 169 in Regulations 69, or *130 pages removed from the interpretation of "ordinary and necessary expenses"* in Article 101).

What the Commissioner in effect says is: Congress had to read Article 561 in Regulations 69, to find out about deductions for corporations, and even though we referred them back to Articles 101-112 to find out about our interpretation of "ordinary and necessary expenses", just the same they should have read Article 562 which dealt with the subject "Donations" regardless of the fact that the Act itself did not recognize any corporate-deductions for "Donations", or for "Charitable and other contributions".

In other words, the Commissioner carries the "reenactment rule" *to everything contained in Regulations*, and if the Members of Congress fail to read every word, to re-classify into proper places,—they are bound by hidden or concealed statements when they repeat the language of one revenue-act in a subsequent revenue-act. With respectful solemnity we say:— "Stop, Look, and Listen!"; The thing is going too far.

Next, we consider the matter relative to Regulations 74 and the specific Article 262 as the Commissioner's reliance.

In those Regulations 74, the Treasury set forth in the Articles 121-132 the interpretation of "ordinary and necessary expenses" as applicable to *all forms of business*, regardless of whether carried on by individual, partnership, corporation, or trust. In Regulations 74 there was no separate Article dealing with corporations (as in Regulations 69, and a reference-back). In Regulations 74, however, the subject of Donations by Corporations finds a placement by the Treasury itself under that section of the Act which deals with "Charitable and other contributions", thus showing (clearly, we assert) that the Treasury and Congress must have interpreted the Article 562 of Regulations 69 as relating to the subject of corporate *donations*, and in no reasonable sense to "ordinary and necessary expenses",—if Article 562 ever was read by Congress.

The matter continued with succeeding revenue-acts. Regulations 77, 86, and 94, dealing with income-taxes under the respective Acts of 1932, 1934, and 1936, restated the Regulations as set forth in Regulations 74 relative to "expenses" and "donations".

But, in Regulations 101 which deals with the Act of 1938 and in Regulation* 103 which deals with the Internal Revenue Code, we find a confirmation of our position and of our construction. These newer Regulations (still attempting to interpret the same, identical language that has stood by repetition in succeeding revenue-acts), now places the kinds of "Donations" which are "business expenses" directly within the Articles that deal with *business expenses*. The matter of donations for "promotion or defeat of legislation" still stands within the Article dealing with "Charitable and other contributions" (Article 23(q)-1 as to corporations) and the very same language has been placed in Article 23(o)-1 which relates to "Contributions or gifts by individuals".

In view of the restricted construction placed upon "ordinary and necessary expenses" in the opinion by Judge

Biggs, it is interesting to observe that continuously, as far back as Regulations under the Act of 1918, the Treasury itself has recognized voluntary gifts or donations by corporations to charities as "ordinary and necessary expenses", by a construction of the term relative to "commendable and helpful" as distinct from a proximate causation.

This petitioner incurred expenses for the "promotion or defeat of legislation" in every year from 1924 through 1930, with reporting of those expenses in the respective tax-returns. Nobody within the Bureau of Internal Revenue conceived the idea that such expenses were non-deductible as being the kind of "donations" that were excludible under Articles 562 and 262 of respective Regulations,—until the Bureau's notice of deficiency dated February 8, 1934 (R. 8-11). It clearly enough was known to the Bureau that they *were expenses, not donations.*

We were not making "contributions" or "gifts" to anybody. We were in a business where contracts required that we pay the expenses, and we were performing our contractual obligations.

B—The Reenactment Rule.

The Commissioner states his basis for litigation by his brief in the court-below as;

"the repeated reenactment of the same statutory provisions amounts to legislative approval of the administrative interpretation of such provision."

Regardless of whether the rule may favor taxpayers at times, the writer of this brief does not hesitate to describe the rule as being the most pernicious and indefensible theory ever finding injection into jurisprudence. Regardless of court decisions that express the rule, erroneous precedents do not make good-law. (See, "The Struggle for Judicial Supremacy", by Hon. Robert H. Jackson, p. 272 *et seq.*, commenting on 96-years of precedents under *Swift v. Tyson*, 36 Pet. 1, being reversed by *Eric Railroad Co. v. Tompkins*, 304 U. S. 64.)

In the case at bar, we find an attempt to carry the reenactment rule to the nth-degree of absurdity. That attempt was repudiated by the Board and by three of the judges in the court-below.

Although judicial decisions politely describe the reenactment rule as being founded upon a "presumption" of knowledge by Congress, the Commissioner in the case at bar makes of it a charge of *negligence* against the 70th Congress (responsible for the Revenue Act of 1928) for a failure to anticipate the interpretation which the Commissioner failed to make from 1924 to 1933 inclusive and first made in the year 1934 (or, six years after the 1928-Act).

As previously stated herein, for all the years 1924 to 1930 inclusive, this petitioner was reporting in its tax-returns the deductions for expenses required under its contracts for "the promotion or defeat of legislation". Nobody in the Bureau conceived the thought that the Article in the Regulations dealing with corporate "donations" had an application to such business expenses,—until 1934. Although nobody in the *Bureau* "knew it", the Commissioner now declares that *Congress* should have "known it", when it reenacted the language for "ordinary and necessary expenses" into the Revenue Act of 1928. Surely, if there is a presumption of knowledge by Congress, there cannot be a presumption of *ignorance on the Bureau's part*.

From time immemorial the statutes of the United States have provided for a judicial review in tax matters. Suits in courts have been recognized as the procedure for determining the judicial interpretation of the revenue-acts in application to taxpayers. Suits in court still are recognized, with the addition (since 1924) of procedure for judicial interpretations short of additional tax-payments, through the Board of Tax Appeals with appellate review by the courts.

In no way can a matter reach the stage of a judicial review, except by a Regulation which is adverse to taxpayers or by an interpretation of a Regulation in an adverse manner to taxpayers. If the Regulations and the interpreta-

tions thereof always were favorable, a "case or controversy" never could arise. Only by *adverse rulings* does a judicial review become possible.

That is our system. Unfortunately, perhaps, it is not possible to obtain an Opinion of the Justices in matters of Federal law, such as pertains in some States. Our system necessitates judicial contests for the interpretation of the Federal laws. In no way can a contest arise, so as to result in a judicial interpretation, except by an administrative ruling against the citizen, that in turn causes the citizen to resort to the courts (or Board).

If a reenactment of the law should cause the administrative interpretation to *become the law*, the entire system for judicial review would be a nullity. Then, the adverse ruling *is the law*, and is not the means for creation of a "case or controversy" (See *Helvering v. Hallock*, 309 U. S. 106).

Yet, observe this fact;—since 1939 the tax system has existed under the Internal Revenue Code, which is a reenactment of the laws as to the matters of judicial processes in tax matters, review by the judiciary as to "cases or controversies", and judicial interpretations as the final word regarding language applicable to the determination of taxes. It would appear that, just as "Congress" never knew of Regulations when enacting former revenue-acts, it likewise never knew of the "reenactment rule" when it enacted the Internal Revenue Code. Or, it is possible that Congress abolished the "reenactment rule", knowingly, by the enactment of the Internal Revenue Code, and thus restored the Judiciary to its proper functions for judicial review, judicial interpretations, and judicial decisions regarding taxes?

However, it may be observed also, that in no year *prior* to 1939 has any Act of Congress abolished the procedure for judicial reviews, despite the announcement by courts of the "reenactment rule". To the contrary, many amendments have occurred relative to the judicial processes,—even to the extent of adding judges by reason of the increased volume of cases, in large measure tax-cases.

The "reenactment rule" could be excused only for relieving the judiciary from the problems of statutory interpretation, by avoidance of responsibility. It served no stabilizing influence, no certainty for a future guidance,—because it always could be disregarded when judges saw fit to tackle the problem and to decide the question contrary to an administrative interpretation by Regulations. A new Regulation could reverse a former Regulation, with judicial approval. It was founded on a fiction or upon presumption which had no factual basis. It constituted an indictment of the Congress. It merits complete repudiation, and *should be repudiated*,—relative to administrative interpretations of laws of Congress. The rule may have a proper place with reference to matters of administrative practice, but it has no place in the realm of *judicial-interpretation*.

The writer of this brief is not embarking alone upon an uncharted sea, nor pioneering in a wilderness, when advancing such out-spoken criticism of the "reenactment rule".

Judge Clark stated in the court-below (R. 65):

"The writer of this opinion has little faith in this rule. He quite agrees with the learned author of an article in the Yale Law Journal who says:

'Among the innumerable fictions which have formed a part of the science of law, that which holds the record for unrealism is the doctrine that where a statute has been reenacted in the same form after an administrative construction, Congress has silently approved and incorporated the existing ruling. Our tax laws are reenacted so repeatedly that this rule is invoked more often than the general statement as to the validity of regulations standing alone. Unfortunately, the reenactment rule presumes an attention on the part of Congress in connection with tax legislation which is more ideal than real. The thought is that Congress, each time it passes a revenue act, has omniscience as to all outstanding regulations and judicial decisions and that it will be thoroughly diligent to correct by legislation

any interpretation with which it disagrees. There follows the thought that inaction is action in that a failure to legislate implies an agreement with all outstanding regulations, without any apparent distinction as to their interpretative or legislative character.

Anyone cognizant of the processes and exigencies of tax legislation is perfectly familiar with the simple fact that any such presumption is not only artificial, but in large part unfounded . . .

Paul, *Use and Abuse of Tax Regulations in Statutory Construction*, 49 *Yale Law Journal* 660, 663-664."

Judge Maris' opinion, with concurrence by Judge Goodrich, deals with Article 262 by agreement with the Board in holding that the Article has no application to the facts in this case. (R. 72-75.)

We agree with Mr. Paul in *Studies in Federal Taxation*, 3rd Series, (restatement of the article in *Yale Law Journal* quoted above) when he states by note at page 426:

"The doctrine reminds one of Tourtonlon, who found 'gravé philosophic insight in a scene from a drama of the poet Mistral, where galley slaves, as they row, believe they see the light of a fairy castle to which they seem quite near. Perhaps, however, the light is but a star. They sing: "Castle or no castle, let us row as if it were there".' Frank, *Law and the Modern Mind*, p. 320 (1930)."

We agree with Judge Learned Hand, when stating in *F. W. Woolworth Co., v. United States*, 91 Fed. (2d) 973, 976 (Cert. Den. 302 U. S. 768):

" . . . To suppose that Congress must particularly correct each mistaken construction under penalty of incorporating it into the fabric of the statute appears to us unwarranted; our fiscal legislation is detailed and specific enough already . . ."

We express agreement with the statement by Professor Griswold (54 *Harvard Law Review* 398, "A Summary of the Regulations Problem," at 400):

"For I wish to advance the proposition that *the mere reenactment of a statute following administrative construction should be given no weight whatever in determining the proper construction of the statute*. I would like to put this in the strongest language possible, for it seems to me that the reenactment rule is the real cause of much of the present confusion in the regulations problem. If the reenactment rule could be frankly abandoned, many of the difficulties which have plagued us here would vanish, and regulations could be dealt with as regulations and without the difficulties that have come from a false statutory analogy." (Italics are Prof. Griswold's.)

This brief will avoid a repetition of analysis, comment, and argument, which so ably have been presented by other writers on the subject, and directs this Honorable Court by reference to:

1 Paul and Mertens, *The Law of Federal Income Taxation* (1934 & Supps.) Sections 3.16-3.20;

Alvord, *Treasury Regulations and the W. Shire Oil Case*, 40 Col. L. Rev. 252;

Surrey, *The Scope and Effect of Treasury Regulations under the Income, Estate and Gift Taxes*, 88 U. of Pa. L. Rev. 556;

Brown, *Regulations, Reenactment, and The Revenue Acts*, 54 Har. L. Rev. 377;

Paul, *Use and Abuse of Tax Regulations in Statutory Construction*, 49 Yale L. J. 660, reprinted with some changes in Paul, *Studies in Federal Taxation*, Third Series, 420;

Griswold, *A Summary of the Regulations Problem*, 54 Har. L. Rev. 398;

84 Lawyers Edition 28 (Note to *Sanford's Estate v. Com.* 308 U. S. 39);

73 Lawyers Edition 322 (Note to *United States v. Missouri Pac. Railroad Co.*, 278 U. S. 269).

Without incurring repetition, however, we analyze facts which are pertinent to this particular case and the Commis-

sioner's charge against the 70th Congress that it *should have known*, when it enacted the Revenue Act of 1928.

The entire House of Representatives was elected in November 1926, with about 65 of the Members not having served in the 69th Congress that enacted the Revenue Act of 1926; some of the Senators were newly elected. The First Session of the 70th Congress did not convene until December 5, 1927. During the 69th Congress a surplus in the Treasury was evident and the "leaders" agreed that the succeeding Congress would enact amendments to the revenue-laws for *reduction in taxes* (See, Report by Chairman of Ways and Means Committee, Report No. 2, 70th Congress, 1st Session, page 1). Prior to the convening-date, the Ways and Means Committee held public hearings from October 31 to November 10, 1927. The Committee introduced a Bill on December 7, 1927 as H.R. 1 (being the first Bill introduced at that Congress), expressing the views of the Committee as regards reductions in the taxes. The Bill passed in the House on December 15, 1927, or eight days after its introduction. Two days prior to that passage-date, or on December 13, 1927, the same Ways and Means Committee introduced into the House, H.R. 7201 which was the Bill which evolved into the Settlement of War Claims Act. That Bill passed in the House on December 20, 1927.

It would appear enough of an impossible task to presume knowledge by the Members of the 70th Congress with regard to the thousands of *Bills* which came before them, without adding as a presumption that they were thoroughly conversant with Treasury Decisions as Regulations and with Treasury Decisions as amending Regulations,—and with interpretations in all manner of other administrative departments.

Thus, by December 20, 1927, both Bills, H.R. 1 and H.R. 7201, stood in the Senate with assignment to the Senate Finance Committee. That Committee saw fit to accord expedition to the H.R. 7201 and the Settlement of War Claims Act was enacted March 10, 1928.

Relative to the H.R. 1, the Senate Finance Committee held public hearings from April 9-13, 1928, with the Bill being referred back to the Senate May 1, 1928 and enactment into law on May 29, 1928.

Regulations 69, construing the Revenue Act of 1926, were promulgated August 28, 1926. Between that date and May 29, 1928, as the enactment date of the Revenue Act of 1928, sixteen separate Treasury Decisions were issued by way of specific amendments to specific Articles of the Regulations 69,—three of those Treasury Decisions being issued while the H.R. 1 was under consideration in Congress. After the enactment of the 1928-Act, additional Treasury Decisions were issued by way of amendments to the Regulations 69, four in 1928, four in 1929, and four in 1931. Although the 1928-Act was enacted May 29, 1928, the Regulations 74 pertinent thereto, did not issue until February 15, 1929 or about two-weeks prior to the termination of the 70th Congress.

During 1929, 1930, and 1931, and after the issuance of Regulations 74, eleven Treasury Decisions were issued, by way of specific amendments to Articles in Regulations 74. Between January 1932 and December 1934, there were nine Treasury Decisions which specifically amended Regulations 69 and nine likewise that amended Regulations 74. During that latter period, revenue-acts of 1932, 1933 and 1934 were enacted, with three new sets of Regulations and with amending Treasury Decisions.

With the observation that Regulations 69 were issued as Treasury Decision No. 3922, it may be interesting to note that, with consecutive numbering, we have reached at the moment of this writing No. 5043.

In addition to all the Regulations and more than 1100 Treasury Decisions, we perceive the interpretation of tax-laws in 44-volumes (1500 pages each) of decisions by the Board of Tax Appeals, and court decisions (carrying only into the year 1940) in 24 volumes (1200 pages each) of "American Federal Tax Reports." Additionally, there have been innumerable publications of "rulings," "opin-

ions" and such, by the Treasury Department of a nature less important than Treasury Decisions.

Hundreds of the court-decisions have found a re-publication as Treasury Decisions, thus giving them an importance equal to direct administrative interpretations. Hundreds of the Board's decisions have received published acquiescence by the Commissioner.

In such a confusion of volume and contradiction, together with the continuous changes in the personnel of "Congress," the presumption of knowledge on the part of the varying membership, so that inaction becomes action by way of approval of Regulations (particularly as the Regulations constantly are being amended by Treasury Decisions), is a thing which becomes unbelievable.

The fallacy of "the theory" has another aspect. Since 1939 we have existed under the Internal Revenue Code. As amendments are proposed in revenue bills, it is done by specific amendments to certain sections or subdivisions of the Code. Regulations 103 purports to interpret the Code and articles therein find amendment by specific Treasury Decisions. In other words, there is no reenactment of the language in a previous revenue-act that has been construed by a Regulation. The new revenue-bills are silent except as they expressly state amendments. It would appear equally justified to declare that a *failure to amend* some unamended section of the Code that had been incorrectly interpreted, constituted an approval by Congress with regard to such unamended portion, as that it approved the language of the Regulation-article which dealt with the amended portion *except for the amendment*. The realm of "presumptions" holds no limits. (Recently so holding, see: *Jones v. Goodson*, 121 Fed. (2d) 176.)

"The theory," also, practically paraphrases the maxim *Ignorantia juris neminem excusat*, into the proposition; Congressional ignorance of an administrative interpretation does not excuse that interpretation from becoming an Act of Congress, when in ignorance of the interpretation the same language of the law is reenacted.

Thus, the failure by a Congress to know of an administrative interpretation of a previous Act of a prior Congress, compels the next Congress to have an Congressional-intent identical with the administrative interpretation of the previous Act. An estoppel is invoked, against Congress and against a judicial interpretation *by the courts*. We seriously wonder about that, when we contemplate the fact that a Board of Tax Appeals was created by an Act of Congress and has functioned now for seventeen years.

The Board was established under the Revenue Act of 1924 and was made quasi-judicial by amendments in the Revenue Act of 1926. It was established, expressly, as "an independent agency" with jurisdiction to review the determinations of the Commissioner. Decisions of the Board, in turn, stand reviewable as to questions of law by circuit courts of appeals. If "the theory" operates, the establishment of the Board as a reviewing agency was a futile effort; the reenactment of the revenue-act, as an approval of Regulations, debars the Board from any interpretation of a revenue act which is contrary to a Regulation. Thus, the Regulations *are the law*, and when Congress granted the right of appeal to taxpayers, the whole thing was an empty gesture. If all that the Board can do, is to ascertain the facts and to apply thereto the Regulation, that is no different from what the taxpayer could get from the Bureau itself. A complete review of a deficiency by an independent agency never was granted. Circuit courts of appeals cannot review questions of law, because the Board cannot decide them if the Regulations cover the subject. If all that were true, we gaze upon seventeen years of operations, with sixteen members of the Board receiving salaries of \$10,000 each, with an organization of more than 100 assistants working with the Board,—all for no purpose except to hear the evidence and apply it to interpretations by Regulations. Why then, we inquire, the provisions for review by the circuit courts of appeals on questions of law? The "defendant" in the Board proceedings is the very same person (Commissioner) *who writes or approves the Regulations*; how can the Board in-

interpret his Regulations contrary to his interpretation *in the very case?* If the Board cannot, there is no "question of law" for a judicial review.

If the Board cannot, then the courts cannot adjudicate in suits for refunds. The Administrative thus has supplanted both the Legislative and the Judiciary.

It is little wonder that this matter of "legislative approval" has received such study and criticism as comes to light in the writings by Mr. Paul, Prof. Griswold, Prof. Sarrey, and the others whom we have cited herein.

The favorite argument for the "reenactment rule" is the idea of "long-continuedness" (as described by Prof. Griswold). Obviously, an administrative interpretation that is favorable to taxpayers is certain to be "long-continued." The only way the question ever can reach the courts is by an *unfavorable* interpretation. If a new regime in the Administration disagrees with the interpretation of predecessors, the judicial processes should not be barred. Only by such a reversal of interpretation may the judicial processes be called upon for action.

Nor, should the "long-continuedness" of an administrative interpretation that is detrimental to taxpayers, without judicial review, carry the presumption of correctness because of the lack of litigation and judicial decision. There are many explanations of non-litigation. Tax-cases usually involve many issues. Settlements may be by a "give-and-take" process, with concessions made on both sides of the table. In the final analysis the settlement is a matter of dollars, a lower deficiency or a lower refund by granting one issue upon the taxpayer's agreement not to litigate the very question that appears to be "long-continuedness."

Then, again, the "long-continuedness" may result from an *interpretation* of the Regulation in a manner favorable to taxpayers. So long as the interpretation remains favorable, no judicial decision can result.

"Long-continuedness" finds at its basis the doctrine of *stare decisis*. But it goes even further, because it imputes

the doctrine to Congress itself, binding it by a lack of litigation or by silence.

If there be any virtue in "long-continuedness" it should have an application to the very case at bar. Why not presume that Congress, when enacting the Revenue Acts of 1924, 1926, and 1928 (and 1932 as well) was cognizant of an interpretation of the Regulations, that they had no application to the facts of our situation,—as to presume (as the Commissioner here insists) that the reenactment approved an interpretation that the Commissioner never conceived until the year 1934?

C.—*The Super-Enactment Rule.*

The opinion of Judge Biggs in the court-below (R. 49, 50) construes the Article 262 in Regulations 74 by the action of a Congress *eight-years later*, the 74th Congress when enacting the Revenue Act of 1936.

That opinion finds a purpose by the 74th Congress to condemn expenses relative to the "promotion or defeat of legislation" when made as *donations*, in a situation where that Congress, for the first time, gave recognition to the right by corporations to deduct gifts to charitable corporations by limitation to 5 per cent of the net income.

That opinion, we respectfully submit, fails utterly to realize the distinction between "donations" and "expenses". The opinion reasons that, if expenses relative to legislation were deemed to be "ordinary and necessary expenses" by the 74th Congress, there would have been no reason for that Congress granting the deduction for *donations*. As the 74th Congress so interprets, declares the opinion, the 70th Congress must have interpreted likewise.

The fallacy lies in even attempting to interpret the thoughts of the 70th Congress by the occurrence of legislation eight years later. We describe such reasoning as the "super-enactment rule" because it binds an earlier Congress by the actions of a later Congress.

But, additionally, we disagree most decidedly with the interpretation even regarding the "mind" of the 74th Congress.

In the first place, the Act of 1936 was *not* the origin (as Judge Biggs states) of that provision. It originated in the Revenue Act of 1935, finding a first suggestion in a minority report of the House Ways and Means Committee.¹ It had been suggested as far back as 1918, that corporations should be allowed deductions for gifts or contributions to charitable organizations.² That proposal was rejected in the Act of 1918. But, such a measure actually was incorporated into the Bill that passed the House in 1921, in the process of legislation into the Revenue Act of 1921. It was rejected by the Senate Finance Committee. The Conference Committee Report stated:

"The House bill extended to corporations the provisions of existing law allowing individuals to deduct contributions made for charitable purposes, limiting the amount of such deductions to 5 per cent of the net income. The Senate amendment strikes out the provision; and the House recedes."³

After the failure of the measure to receive approval in the Revenue Act of 1921, the subject was discussed at successive hearings on subsequent revenue legislation.⁴ In 1935 the provision was adopted into the Bill upon the floor of the House, the Committee not having made any recommendation.

The only way that the amendment of 1935 changed the previously existing situation was, by authorizing deductions for payments made to charities, even though the payments *bore no relation to the operation of the business*. The 5 per

¹ House Report 1681, 74th Congress, 1st Session, p. 20.

² Seidman's Legislative History of Federal Income Tax Laws, 286.

³ House Report No. 486, 67th Congress, 1st Session, p. 36.

⁴ Seidman's, Legislative History of Federal Income Tax Laws, 287.

cent limitation relative to net income, was identical with all previous suggestions back to 1918 when the proposal had its origin. The limitation—"no part of the net earnings of which inures to the benefit of any private shareholder or individual"—also was found in the earlier suggestions. The only new language was,—“and no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation”. New also, was a clause authorizing a check-up by the Commissioner through rules and regulations. Thus, we find evolving into the Revenue Act of 1936 an entirely new provision of law:

“23 (q). Charitable and other contributions by corporations.—In the case of a corporation, contributions or gifts made within the taxable year to or for the use of a domestic corporation . . . organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes or the prevention of cruelty to children . . . , *no part* of the net earnings of which inures to the benefit of any private shareholder or individual, *and no substantial part* of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation; to an amount which does not exceed 5 per centum of the taxpayer's net income as computed without the benefit of this subsection . . . ” (Italics added.)

The analysis by opinion of Judge Biggs distorts, we submit, the intention of Congress even in 1935 and, it should be noted, this case at bar involves deductions of 1929 and 1930. That analysis also glides over the actual language used by Congress.

Congress was not limiting corporate payments to charities where the payments constituted “ordinary and necessary expenses”. Rather, it was granting a concession for charitable donations in instances where the payments *had no relation to business expenses*. The motive for the concession is expressed in that Minority Report⁵:

⁵ See Note 1.

“If corporations are public spirited enough to make contributions to charities, we believe their contributions for such purposes should be exempt from taxation exactly as is done in the case of individuals.”

May it be noted further, that by the very language quoted above, Congress did not deny the deduction if *some part* of the charities' activities involved legislation. The denial of the concession by way of deduction was to occur only if a “substantial part” of the activities had legislative purposes. The distinction is clearly expressed:—“no part” of the earnings inuring to shareholders and “no *substantial part*” of the activities involving legislation.

A hospital, a college, a community chest, even a Red Cross, might seek the grace of legislation for its activities. Funds derived through contributions might find such a use. But, only where a “substantial” part of the activities were directed toward influencing legislation, was the concession to be denied.

Here was something which had nothing to do with the business itself. For more than twenty years corporations had been obliged to bear taxes upon so much of the net income as was contributed to charities, in instances where there was no business relation. In effect, a corporation had been penalized for gifts to charity. This voluntary concession by Congress sought the encouragement of such gifts through tax exemption within limitations.

We submit that such a discretionary concession by the 74th Congress has no bearing whatsoever upon the question presented in this case, namely with regard to the interpretation of an Act of the 70th Congress.

It no more would be fair to declare that the 1935-amendment shows that the 74th Congress has condemned “lobbying”, than to say that it deemed improper the fact that net earnings might inure to a private shareholder in a charity. A school, a college, or a hospital, may have private shareholders; 99 per cent of the activity may be educational or charitable. But the fact of even a small phase of earnings

inuring to the benefit of a private shareholder, destroys the tax-exempt nature of the contributions. That is not because it is morally wrong or illegal that a private shareholder should profit. Arbitrary or not, that merely is a condition that Congress has stated, and the condition must be met when the concession is sought. Arbitrary or not, a similar condition applies where a "substantial part" of the charities' activities involve the influencing of legislation.

Note how Regulations 94 interpreted that change in the law, by Article 23 (q)-1:

"A corporation is entitled to deduct from gross income for a taxable year beginning after December 31, 1935, contributions or gifts to organizations referred to in section 23(q), *whether or not such contributions or gifts constitute business expenses*, but only to the extent provided in that section. . . ." (Italics added.)

As evidencing the value of "interpretations by regulations" it might be noted also, that the remainder of the Article proceeded to interpret the new provision as a limitation to 5 per cent of the net income even where the gift held a relation to a business,—such as to a hospital where the employees received treatment. Here was new legislation of a remedial nature, extending deductions,—yet it finds interpretation by way of restriction as compared with the previous Acts.

D.—The Reasoning by Opinion of Judge Maris Relative to Article 262 of Regulations 74 and the Sunset-Scavenger Case, is Sound and Should Be Approved.

The opinion of Judge Maris (R. 72-75) so thoroughly and convincingly covers the Article 262 and the decision in *Sunset Scavenger Co. v. Commissioner*, 84 Fed. (2d) 453, (the Commissioner's sole reliance before the Board), as to permit our avoidance of argument by repetition. Therefore, we respectfully make reference to the Record in that regard, and we discuss that case only briefly.

That decision is based upon "the reenactment rule" wholly, so our discussions of that rule apply to that decision.

Additionally, however, there are such clearly marked distinctions between the facts in the case at bar and the situation in that decision, that they merit comment.

Special legislation, such as we sought under contracts which caused our actions to be the very business in which we were engaged is decidedly different from a matter of combatting *general* legislation,—such as the City Ordinance pertinent to the collection of garbage in the *Sunset-Scavenger* case, as a matter of such pronounced public-interest.

The business itself of the Sunset Scavenger Company was the collection of garbage, a matter which, under the police powers, the city-fathers had the right to control in the interest of the public health.

On the other hand, so far as concerned the German-nationals whom we represented, the Trading with the Enemy Act *was special legislation*, because it dealt specifically with the seizure of their property in the United States. It was special legislation *as to them*, even though it found a public purpose as a war-measure.

That Act expressly stated in Section 12:

"After the end of the war any claim of any enemy . . . to any money or other property received and held by the alien property custodian . . . shall be settled as Congress shall direct."

That Act recognized the existence of claims by seizures and recognized, further, for special legislation to settle the claims.

The Settlement of War Claims Act was special legislation as to the American-claimants and it was special legislation as to the German-claimants. Obviously, the claimants so specially affected, were the proper persons to advocate the terms of the special legislation by way of settlement, just as with any Bill relating to any particular person. Who else is to urge it and discuss it with the Members of Congress, *than the person himself?* For obvious reasons, the

persons who were located thousands of miles away in Germany had to engage representatives in the United States.

But, one other fact merits mention. Throughout the entire history of revenue-laws, there never has been either a provision of law or a *regulation by way of interpretation*, to the effect that the expenses of individuals, partnerships, or trusts which engage in business, are non-deductible as relating to "the promotion or defeat of legislation". If the thing held the slightest aspect of inherent wrong, there is no reason for permitting the deductions to one form of business and not permitting it to another,—such as corporations. Perceive the pertinency of that statement *to this case*. Our contracts were made with an *individual* (R. 34) and he assigned them to the corporation. (R. 34)

If the assignments had not been made, the deductions would have been recognized to the individual although expenses for legislation (See, *Lucas v. Wofford*, 49 Fed. (2d) 1027). That decision would have controlled the matter if the assignments *had not been made*; but, declares the Commissioner, the *Sunset-Scavenger* case controls the matter *because the assignments were made*,—and "the reenactment rule."

We respectfully inquire: Can there be the slightest justification for "the reenactment rule", when it means the application of one rule of law to two or three persons engaged in business through the partnership-form and an entirely different rule when those same persons conduct their business through the corporate-form? Can there be any sense for it, to change the applicable legal principles when a single-person operates as a corporation instead of by a sole-proprietorship?

We submit that the questions convey their own obvious answers and that, when we describe "the reenactment rule" as being carried into the realm of "absurdity" by the Commissioner's contentions, our language is most conservative.

III.

Concluding explanation.

We submit to this Honorable Court that the judgment of the court *en banc* should be reversed; that a circuit court of appeals for the Third Circuit Comprising Judges Maris and Goodrich as a quorum thereof should be directed (pursuant to the Motion filed by the petitioner in that court, R. 76-78) to order a judgment by way of affirmance of the Board-decision; and that the reasoning by opinion of Judge Maris (R. 66-75) and by opinion of the Board (R. 13-22) merit the approval of this Court by the entry of any other form of appropriate Judgment for the Petitioner.

We urge further, that the court *en banc* was lacking in authority to reverse the Board-decision upon new issues that were not presented to the Board and, in that regard, we refer to the citation of precedents at pages 23 and 24 herein.

The foregoing portion of our Argument covers the issue that was presented to the Board, was appealed by the Commissioner to the Third Circuit, and was decided favorably to the petitioner by a majority of three judges in the court *en banc*. The additional length of this brief is occasioned wholly by the injection of the new-issues in the court below; our brief would stop at this point, except for the compulsion that we discuss those "new issues".

ARGUMENT

Part 2. The New Issues in Appellate Court

ARGUMENT.

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I.

Introductory.

This remaining portion of our brief is occasioned by the injection of "new issues" by the opinions of Judges Biggs and Clark in the court below and an entry of judgment predicated on their conclusions regarding those "new issues". The reasoning in those opinions can be expressed by a Syllogism:

Major Premise:—Criminals are taxable upon their entire gross receipts from their criminal operations, without deductions for their expenses incurred in performance of their crimes.

Minor Premise:—The petitioner was a criminal, because,

1. It operated under contingent contracts for the procurement of legislation, or
2. It sought for its principals "favor" legislation, in distinction from "debt" legislation, or
3. Representation of enemy-aliens in the procurement of legislation for the return of their properties, seized under the Trading with the Enemy Act, was illegal, or
4. The contracts were void as being against public policy.

Conclusion:—The deduction of the expenses is not allowable.

When petitioning this Court for Certiorari we had not the slightest interest in the establishment of a precedent relative to the considerations involved in the Major Premise of that syllogism. We are not concerned in the least degree as to how the taxes of the criminals may be determined,

whether they range from the organized murderers such as "Murder Inc.," down to the innocent seller of food products who operates his business after the expiration of his Victuallers License, negligent in the failure at renewal.

If the Bureau of Internal Revenue desires to be "an accessory after the fact" by participating in the fruits of the crimes through the process of "taxation", that is the Bureau's concern.

It has been the general understanding that Taxation held as a fundamental basis the idea of imposition of taxes relative to the "ability to pay" the taxes, and we can perceive no "ability to pay" relative to the criminal whose expenses exceed his receipts. The only method within our perception, whereby he can find such "ability to pay" is, by the continuation of his criminal pursuits in the hope that they eventually may be profitable. There again, if that is what the Bureau desires to encourage, it is the Bureau's concern.

We sought the consideration by this Honorable Court because, in addition to the importance of questions, an innocent citizen, engaged upon an honorable venture, is classified among the criminals by a lower court, without the slightest provocation or excuse, and only by injecting into a case issues that were not properly before that court. We owe it to ourselves and to other citizens, to pursue and seek Justice, without regard for monetary considerations.

The final decision in this case will not constitute a precedent to affect our taxes in any years prior or subsequent to the year here involved, 1931, because all other years in which we incurred similar expenses have been closed by the Bureau without questioning the expenses.

We sought the jurisdiction of this Court by reason of the importance of many questions involved herein, and that importance finds clear confirmation in the interest expressed relative to the opinions in the lower court, with unanimous criticism of the two opinions to which we object:

54 Harvard Law Review, 698, 699; Note on decision below;

54 Harvard Law Review, 852-866; Note on decision below;

8 University of Chicago Law Review, 774-779; Note on decision below.

The Conclusion in the syllogism is erroneous, because *both* the Major Premise and the Minor Premise are *false*.

Our main interest, however, is in the falsity of the Minor Premise. Accordingly, we will devote our discussion mainly to that Minor Premise, dealing also with the Major Premise by way of rendering full assistance to this Court.

II.

History of The Settlement of War Claims Act of 1928 With Relation to Petitioner's Connection Therewith.

The actual fighting in World War No. 1 ceased with the signing of the Armistice on November 11, 1918, but the state-of-war as between Germany and the United States continued for two and one-half years thereafter. That war finally was terminated by Congress, by Joint Resolution of July 2, 1921 (42 Stat. L. 105). By Section 2 of the Trading with the Enemy Act (40 Stat. L. 411) the words "end of the war" were defined "to mean the date of proclamation of exchange of ratifications of the treaty of peace, unless the President shall, by proclamation, declare a prior date, in which case the date so proclaimed shall be deemed to be the "end of the war" within the meaning of this Act."

The Treaty between The United States and Germany, was signed at Berlin August 25, 1921. By Presidential Proclamation of August 25, 1921, it was declared that the war with Germany terminated on July 2, 1921.

Section 3 of the Trading with the Enemy Act prohibited during the war all trade, dealings, and intercourse, as between persons in the United States and an "enemy" as defined in that Act.

By Section 2 of that Act the word "enemy" was defined to mean;

"Any individual . . . of any nationality, resident within the territory . . . of any nation with which the United States is at war, or resident outside of the United States and doing business within such territory of any nation with which the United States is at war or incorporated within any country other than the United States and doing business within such territory. . . ."

Authority was granted the President, by proclamation, to include within the term "enemy", individuals wherever resident or wherever doing business, who might be "natives, citizens, or subjects of any nation with which the United States is at war, other than citizens of the United States".

The Act authorized the seizure of the property of "enemies", through an Alien Property Custodian.

It will be noted that the definition of "enemy" placed dependency upon the fact of *residence* of the person, rather than his nationality. Accordingly, as the armed forces of Germany occupied territory in France, Belgium, and other allied or neutral countries, the persons who were resident within those occupied territories automatically became "enemies", with their properties in the United States subject to seizure under the Act. The definition also found extension through Presidential action from time to time, with the result that some 5,000 persons experienced internment in the United States and their properties were seized.

At the height of the seizures the total of property in possession of the Alien Property Custodian amounted to approximately 800-millions of Dollars (the exact amount never was accurately determined).¹

In Section 12 of the Trading with the Enemy Act was this important provision (important from the standpoint of this case) :

¹ At the time of the Settlement Act it amounted to about 250-millions.

“After the end of the war *any claim* of any enemy or of an ally of enemy to any money or other property received and held by the alien property custodian or deposited in the United States Treasury, *shall be settled as Congress shall direct:*” (Italics added)

After the signing of the Armistice and prior to the Joint Resolution of July 2, 1921 (*supra*), and with the state of war still in existence, Congress enacted three successive Acts by way of amendments to the Trading with the Enemy Act, ordering releases as to the properties which had been seized from “enemies” *in certain, particular situations*.

An Act of July 11, 1919 (41 Stat. L. 35) provided in part:

“ . . . That in respect of all property heretofore determined by the President to have been held for, by, on account of, or on behalf of, or for the benefit of a person who was an enemy or ally of enemy solely by reason of residence in that portion of the territory of any nation associated with the United States in the prosecution of the war which was occupied by the military or naval forces of Germany . . . and that such person is a citizen or subject of such associated nation, then the President, without any application being made therefor, may order the payment, conveyance, transfer, assignment, or delivery of such money or other property held by the Alien Property Custodian . . . to the said enemy. . . . And the receipt of the said enemy . . . shall be a full acquittance and discharge of the Alien Property Custodian or the Treasurer of the United States as the case may be, and of the United States in respect of all claims of all persons heretofore or hereafter claiming any right, title, or interest in said property, or compensation or damages arising from the capture of such property by the President or the Alien Property Custodian . . . ”

That Act made restoration to persons who were “enemies” only because of residence in the occupied-territories and whose allegiance was to an “associated nation”. But, it will be observed, Congress recognized the *existence of claims* resulting from the seizures, and insisted that res-

tations should constitute the *release and discharge of claims*. May it be noticed, also, that the Act recognized that the properties seized, had been "held for, by, on account of, or on behalf of, or for the benefit of a person who was an enemy".

We will discuss later herein the history of the Trading with the Enemy Act, but we emphasize at this point; that Act was enacted by the 65th Congress, while the 1919-Act was enacted by the 66th or succeeding Congress. In the very first legislation after the Armistice, we find confirmation in two regards,—the trustee nature of possession by the Alien Property Custodian, and recognition by Congress that claims existed. That was in 1919.

An Act of June 5, 1920 (41 Stat. L. 977) again amended the Trading with the Enemy Act (Section 9) so as to authorize restorations to certain, various other classes of claimants (eight categories in all). Those restorations were to be "without any application being made therefor" and, as with the 1919-Act, the receipts constituted "a full acquittance and discharge . . . in respect to all claims of all persons . . ."

An Act of February 27, 1921 (41 Stat. L. 1147) covered restorations to certain women who had married Germans or Austrians, and amended Section 9 of the Trading with the Enemy Act.

After the Joint Resolution of July 2, 1921 (*supra*) only one other Act for partial restoration occurred, "The Winslow Act" of March 4, 1923 (42 Stat. L. 1511). That Act amended Section 9 of the Trading with the Enemy Act and added new sections (20 to 24 inclusive) to the Trading with the Enemy Act. By the Winslow Act provision was made, for the first time, for restorations to German and Austrian Nationals,—that is, to "enemies" who were residents of those countries; but, the payments were limited to \$10,000. in each instance. That Act disposed of a large number of the smaller claims and made restitution to all others up to the \$10,000. limit. That Act, also, permitted annual pay-

ments of income of claimants, up to a \$10,000. limit. The Section 23, thus added to the Trading with the Enemy Act, is significant;

“The Alien Property Custodian is directed to pay to the person entitled thereto, from and after the time this section takes effect, the net income, dividend, interest, annuity, or other earnings, accruing and collected thereafter, *on any property or money held in trust for such person by the Alien Property Custodian* or by the Treasurer of the United States for the account of the Alien Property Custodian, under such rules and regulations as the President may prescribe; but no person shall be paid, under this section, any amount in excess of \$10,000 per annum.” (Italics added)

We respectfully direct the attention of this Court to that italicized language, and we ask comparison with Record, p. 23, where the petitioner's contract of representation is set forth. We quote from the contract-form;

“to protect the interest of the Claimant in *moneys and/or properties now held in trust for the Claimant by the Alien Property Custodian . . .*”

The petitioner's services were engaged by contracts beginning in the year 1924 (R. 30) and the very form of *contracts* took a position that was identical with the position of 67th Congress which enacted the Winslow Act, in practically the identical language of the Winslow Act. The claimants were the *beneficiaries under the trusts* and we were representing their rights and interests as such beneficiaries, seeking a judgment with regard to their *equitable rights*.

Yet, declares the opinion of Judge Biggs (R. 46),—“The contracts between the taxpayer and its clients were to procure “favor legislation” as distinguished from “debt legislation”. The performance of Equity may rest upon a sound discretion, but it does not depend upon “favor”.

Except for an Act of May 7, 1926 which made slight clarification to Section 9 by adding restoration for persons who had become citizens of neutral countries and had acquired their seized-properties while bona fide residents of the United States, there were no amendments to the Trading with the Enemy Act between the Winslow Act of 1923 and the Settlement of War Claims Act of 1928.

Five years elapsed after the Armistice, before the German and Austrian *nationals* (residents, citizens, and subjects of those countries) received any restoration (the \$10,000 limit by the Winslow Act); five years more elapsed before provisions were made by the Settlement of War Claims Act for restorations to the 80 per cent extent of those provisions,—to the *nationals*.

Our contracts were with the *nationals* of those countries, and our engagement in their behalf began in 1924, or three years after Peace and the restoration of friendly relations through the Treaty of Berlin.

We have felt the necessity for mentioning the foregoing facts, because in the court-below the Commissioner's attorney tried to disparage or minimize the importance of our representation, asserting that because Congress made provisions for restoration in restricted instances, our services were not necessary and amounted to nothing.

It would seem to suffice, that the *German nationals* deemed our services so essential that they contracted for our representation.

The necessity for American-representation on behalf of the Germans, will appear clear by a further recital of the history.

The Treaty of Berlin (42 Stat. 1939) (Treaty Series, No. 658, Government Printing Office, 1922) included as a preamble, the Joint Resolution of July 2, 1921 as to Sections 2 and 5. The pertinent part of Section 5, as included in the Treaty, was;

“All property . . . of all German nationals, which was on April 6, 1917, in or has since that date come into

the possession or under the control of, or has been the subject of a demand by the United States of America or any of its officers, agents, or employees . . . shall be retained by the United States of America and no disposition thereof made, except as shall have been heretofore or specifically hereafter shall be provided by law *until such time as the Imperial German Government . . . shall have respectively made suitable provision* for the satisfaction of all claims against said Governments respectively, of all persons, wheresoever domiciled, who owe permanent allegiance to the United States of America and who have suffered, through the acts of the Imperial German Government . . . since July 31, 1914, loss, damage, or injury to their persons or property, directly or indirectly . . . " (Italics added)

That restriction by Congress, that the property in possession of the Alien Property Custodian would not be returned, until the German Government had made "suitable provisions" for the payment of the claims against Germany by American citizens, became the crucial element in the entire matter of legislation for return to the Germans; because of it, it became necessary for the Germans to engage the services of representatives in the United States (such as the petitioner); because of it, the matter of legislation by a Settlement Act became a contest between the two groups of claimants (American against Germany, and German against the United States), both waging their contest through representatives or agents, with the Congress in the status of court or judge. The representatives of the American-claimants pleaded with Congress to provide the "suitable provisions" by the confiscation of the properties of the Germans in satisfaction of the American-claims; the representatives of the German-claimants (including the petitioner through its attorneys and agents) pleaded that the German-properties be restored and that the American-claimants be cared for in some other way. That situation of an impasse continued into December 1926.

The solution came (eventually the Settlement of War Claims Act itself) because the representatives of the two

groups of claimants, compromised their disagreements and *agreed upon the kind of Act which Congress should enact.*

We quote from House Report No. 17, 70th Congress, 1st Session, being the Report presented by Chairman Green when introducing into the House the Bill which eventually became the Settlement-Act, page 4 of that Report:

“It was essential, in the judgment of the committee, that the bill should provide for—

(1) The settlement of the claims of the United States and its nationals against Germany and its nationals;

(2) The settlement of the claims of Germany and its nationals against the United States;

(3) The return of the property held by the Alien Property Custodian which was seized during the war as the private property of citizens of countries with which we were at war; and

(4) The temporary retention of sufficient of the German property to reasonably insure the payment of the American claims and the return of the property thus temporarily withheld as the American claims are paid.

But it was not practical to do this unless concessions and compromises should be made by the respective claimants. Recognizing this, *these parties and their representatives voluntarily got together and agreed upon the concessions to be made by each. The present bill proposes to carry out this agreement.*” (Italics added)

Chairman Green made a more extended statement upon the Floor of the House (Cong. Rec. Vol. 68, Part 1, page 594):

“At the fall session of the committee further hearings were had for about 10 days. At the close of the hearings, when it seemed as if our labors might again have no result, I made a suggestion to the claimants. In substance, I stated that the hearings so far seemed to have resolved into *a contest between the German claimants on one side and the American claimants on the other*, each insisting, in effect, that their claims

should be paid in full and the other side should wait indefinitely; that it appeared to me that as long as this attitude was continued there was little hope of a settlement; but that *if the claimants were disposed to make mutual concessions and agree that the payment of an equitable proportion of the claims on each side should be deferred*, that I thought that by making an appropriation only for the payment of those items for which it was generally conceded our Government was liable, the committee could work out a bill. I confess that at the time I made this suggestion I had little hope that it would be accepted. *It required a mutual spirit of compromise, . . .* I was, however, agreeably surprised over the manner in which the suggestion was received. The claimants, *through their representatives*, immediately conferred with each other and in a short time came to a *complete agreement . . .* All the claimants, so far as I know, now unite in support of the bill and are earnestly urging its adoption . . .” (Italics added)

The complete statement by Chairman Green, at the close of the House hearings, will be found at page 620 et seq., Vol. 4, Return of Alien Property, Hearings before the Committee on Ways and Means, 69th Congress, Interim First and Second Sessions, (Government Printing Office publication).

The signed-agreement will be found at page 129, Return of Alien Property, Hearings before the Committee on Finance United States Senate, 69th Congress, Second Session, (Government Printing Office publication). The agreement was introduced as part of the record on January 13, 1927. The signatures were those of “William P. Sidley, For the American Claimants, and W. Kiesselbach, For the German Claimants,” each representing certain groups of claimants. Mr. Sidley was Chairman of an organization, “American War Claims Association” (P. 20, Senate Finance Committee hearings, January 23, 1928); Mr. Kiesselbach was the German commissioner on the Mixed Claims Commission and particularly represented the German ship-owners (P. 181, Senate Finance Committee hearings, January 14, 1927).

That agreement publicly was approved by the petitioner on behalf of the claimants which it represented, by statement of the petitioner's attorney (R. 31) (Frank W. Mondell), to the Senate Finance Committee, (Pp. 1-20, Senate Finance Committee hearings, January 23, 1928).

The very title of the Bill as first introduced into the House and as carried through into the final Act, was expressive of that agreement between the respective claimants;—"To provide for the *settlement of certain claims* of" (American nationals against Germany and nationals of Germany against the United States) "and for the ultimate return of all property held by the Alien Property Custodian."

The inquiry might be made;—Why did the German nationals have to engage the services of American-representatives? Why did they not act through diplomatic channels?

Conclusive answers to those questions are found in Senate Document 173, 69th Congress, 2d Session, entitled "American War Claims Against Germany," and comprising diplomatic correspondence between July 1921 (after the Joint Resolution terminating the war) and December 1926. As briefly as possible, we quote from that document:

Page 4. The American Commissioner at Berlin (Dresel) to the Secretary of State (Hughes), Berlin, July 22, 1921:

" . . . Rosen requested me to consult Department urgently as to advisability of giving publicity to memorandum . . . He requests me also to suggest that simultaneously with publications in America a declaration might be issued stating the intention of the United States to restore German property in the hands of the Alien Property Custodian. He said this would have most favorable effect on German people and would be a distinct success for the government which they so much needed. I discouraged him on possibility of such a statement pointing out that it would be an anticipation of the action of the Congress and possibly unlawful. It may be possible to give an assurance that the President will recommend such action to Congress but I did not suggest it to Rosen . . . "

Page 5. Secretary Hughes replied; July 23, 1921;

" . . . You correctly stated position as to property in hands of Alien Property Custodian, as Congress alone has power to deal with that matter . . . "

Page 6. (Dresel to Secretary Hughes, July 27, 1921);

" . . . As to American decision that a declaration in regard to alien property custodian fund was impossible at present, Rosen expressed regret but stated that he understood the reasons for American attitude . . . "

Page 13. Secretary Hughes to Dresel, August 20, 1921;

" . . . The Administration is fully appreciative of the considerations entertained by Germany with respect to property sequestered here, and desires a just and reasonable settlement. There is nothing, however, for Germany to gain by opposing the terms of the Peace Resolution or by insisting on anything which could be claimed to be a departure therefrom in the proposed treaty.

It is earnestly urged, with full regard for all the circumstances, that the signing of the Treaty as proposed by this Government . . . will pave the way for consideration of the questions relating to property sequestered here which the President desires to be dealt with upon the most fair and righteous basis. It is hoped that Germany's attitude toward this subject will not put obstacles in the way . . . "

Pages 14 to 33 inclusive cover diplomatic correspondence from February 22, 1922 to August 10, 1922, relating to the establishment of the Mixed Claims Commission for adjudication of claims by Americans against Germany. At page 22 we quote from Ambassador Houghton to Secretary Hughes;

" . . . the German Government believes itself justified in the expectation that the conclusion of the agreement in question will open the way to a speedy return of the German property retained in the United States to its legal owners." (The document shows no reply)

The Mixed Claims Commission was established as the result of agreement executed August 10, 1922. (Treaty Series, No. 665, Government Printing Office, 1922). That agreement contained no method for the payment of the awards. (See, House Report No. 17, *supra*, p. 12)

While that Commission was engaged in its investigations, Germany went, in effect, "into the hands of a receiver, and the Allies were confronted with the task of collecting from a debtor unable to pay the total demands. The Dawes committee of experts was constituted to determine how Germany could pay and the annual payments which could be made . . . Although the United States was not a party to the agreement putting the Dawes plan into effect . . . it could support the Dawes plan and assist in making it successful . . . Accordingly, the United States was represented at the Paris conference which had been called for the purpose of determining upon a division of the payments to be made by Germany under the Dawes plan." (House Report No. 17, *supra*, pp. 12, 13)

The Dawes Plan was proposed April 9, 1924. The Paris Agreement was of January 14, 1925. (Included in document, *supra*, "American War Claims Against Germany.")

It would appear to be self-evident that the German foreign-office was in no position to assert claims on behalf of its nationals under such circumstances as--the financial collapse of its government, the "suitable provisions" clause in the Treaty of Berlin, the inability to meet awards of the Mixed Claims Commission. Nevertheless, after the adoption of the Dawes Plan and the Paris Agreement, the German Ambassador at Washington wrote Secretary of State Kellogg, with the suggestion that the Dawes Plan and the Paris Agreement made the "suitable provisions" and that the proper time had arrived for the return of property from the Alien Custodian. His letter was dated August 6, 1925 and Secretary Kellogg replied by letter of May 4, 1926 (See, document, *supra*, "American War Claims Against Germany", pp. 33 to 40 inclusive). Secretary Kellogg's letter concluded;

"... The question of policy is, of course, separate and distinct from the question of law and, as appears above, has been reserved for determination by the Congress, which body, as Your Excellency is aware, is now considering that question."

At the time the Secretary replied to the Ambassador, *nine months* had elapsed, with his statement correct at the date of reply.

In fact, between December 7, 1925 and March 29, 1926, fifteen Bills were introduced in the House and nine in the Senate, before introduction of the "Mills Bill" on March 29, 1926 as expressing the views of the Ways and Means Committee. Hearings were held by that Committee from April 5 to May 5, 1926, and further hearings for ten days in November 1926.

On November 19, 1926 the petitioner's attorney, Frank W. Mondell, appeared before the Ways and Means Committee, speaking on behalf of German-claimants. He so stated and the Committee so understood.

At the Record in this case, page 31, mention is made of two documents, Exhibits "B" and "C", both of which were written by Messrs. Martin and Clark, and represent part of the services which they performed for us and for which they were compensated by the amounts of deductions here in dispute. The Exhibit "B" was introduced in the Senate as a Senate Document. Mr. Mondell himself presented the Exhibit "C" to the Ways and Means Committee on the date November 19, 1926 and the Exhibit "C" was printed by the Committee as a part of the hearings. It will be found at pages 307 to 331 in Return of Alien Property-No. 4, Hearings before the Committee on Ways and Means, 1926, Government Printing Office.

At that same time, members of the Committee insisted that there also be printed with the hearings, a document which Mr. Mondell had compiled and had delivered in document form to members of the Committee. That document was entitled "Private Property in Time of War" and it appears at pages 293 to 307 in that same No. 4. The docu-

ment itself carried no name by way of authorship because, as Mr. Mondell told the Committee, he did not consider that he was an "author" because he merely arranged the writings of other persons.

The document Exhibit "C" was frankly described by Mr. Mondell to the Committee as containing views with which he agreed and which were favorable to the position of the German-claimants whom he represented.

If any Member of the Committee had deemed the fact as having the slightest importance or significance, he was free to question Mr. Mondell with regard to the connection between Messrs. Martin and Clark, and the petitioner. Nobody saw fit to do so, but would have been told if they inquired.

From the fact that the Exhibit "C" did not carry on the cover some such statement as "Printed and paid for by Textile Mills Securities Corporation, which publishes same as argument on behalf of German-claimants", the opinions of Judges Biggs and Clark find something "suspicious" or "sinister" in the publication.

To the contrary, it was presented to the Committee voluntarily by our attorney, the Committee could have had any information desired, and we had not the slightest reason for any form of concealment.

The very same document was printed as part of the hearings and was free for anybody in the public.

Furthermore, when we submitted the Exhibit "C" with the Stipulation, we did so for the purpose of showing the *kind* of work which Messrs. Clark and Martin performed for us. Both documents were legal treatises or briefs, showed the sources for all statements, and no more constituted "propaganda" than does this brief itself.

The Exhibit "B" dealt with matters from the historical aspect of former treaties; the Exhibit "C" dealt with the subject of the confiscation of former-enemy property in *peace-times*, the question before the Congress being whether it would *then* confiscate (1925-1928).

The Exhibit "B" was printed solely as a Senate Document. How far the Exhibit "C" was distributed publicly, we have no present means for knowing, but we believe the probability to be that it was distributed in the same identical way as Mr. Mondell's own write-up—mainly, to Members of Congress as a more convenient method of their reading (if they desired) than by reading the very same thing in small print *right within the printed record of the hearings*, presented to Congress by our own attorney.

There was not the slightest concealment on our part; nor was there any reason why we would desire to conceal. The bodies of both documents spoke for themselves, just as with any brief. Who wrote them and who paid the authors, were unimportant details that could not have the slightest effect upon the value of the legalistic analysis.

Why was it necessary that we utilize a "publicity organization" like that of Ivy Lee? Solely, wholly, and only because the American claimants were traveling in 1925 and 1926 the length and breadth of the Country, urging the confiscation of our principals' properties so as to supply the "suitable provisions" in satisfaction of claims by American-claimants against Germany. They asserted that the Dawes Plan and the Paris Agreement, following the complete collapse of Germany financially, did not make for "suitable provisions". They perceived as "the easiest way" the use of the seized properties in payment of their claims against Germany. Properly, in a recognition of the obligations under our contracts, we bore the additional expenses that the actions by the American-claimants necessitated. The American-claimants were the constituents of the Members of Congress; the German-claimants had nobody to whom they could address the justice of their cause—except to the Members of Congress through their contract-agents.

Every dollar of added expense came out of us, by force of our contracts. We had no reason for incurring expenses, except as we felt compelled to do so. An "Ivy Lee" never

would have been an event in this matter, except by the compulsion of the American-claimants.

And, may it be noted, the Commissioner agreed with us by the Stipulation that all of that was "necessitated". (R. 30)

III.

The Trading with the Enemy Act, in relation to the Settlement of War Claims Act.

The two Acts are so closely related as to necessitate discussion of the two Acts, for a fair understanding of the "new issues".

The first was an Act of deprivation, the second was an Act of restoration. The first was a war-measure, the second was a peace-measure resulting from the effects of war.

The Act of deprivation specifically recited;

"After the end of the war any claims of any enemy . . . shall be settled as Congress shall direct."

That language embodied clear meanings and notices;

1. The negotiation of treaty should not attempt to include any agreements or concessions regarding the property seized. (That meaning again was emphasized in the Joint Resolution of July 2, 1921 whereby Congress declared the war terminated)
2. Nobody in Administrative departments should make any commitment, because Congress had reserved complete control. (That meaning finds a recognition in the diplomatic correspondence cited in the previous subdivision of this brief)
3. The direction of a claim by an "enemy", either to the Judicial or the Administrative branch of our Government, would be wholly futile and ineffective, because they possessed no authority in the matter. (Again, we refer to the diplomatic correspondence)
4. "After the end of the war" Congress itself would entertain claims and would settle "as Congress shall direct".

As clearly as language could state the matter, we submit, the "enemies" were told—"Bring your claims here to Congress, after the war is ended, and not elsewhere. We will settle those claims as we see fit."

The Trading with the Enemy Act was not legislation for confiscation; it was for sequestration.

So declared Secretary Hughes. (See, letter to Dresel, August 20, 1921, *supra*.)

But, we will permit Congress itself to speak, starting our citations by the statement of Chairman Green when reporting the Bill that finally became the Settlement of War Claims Act.

In his Committee Report for the House Ways and Means Committee dealing with the Settlement of War Claims Act, (House Report No. 17, 70th Congress, 1st Session) Chairman Green states at pages 5 and 6:

"The text of the trading with the enemy act as originally enacted, the reports of the committees accompanying the bill, the discussion on the floor of both Houses of Congress, and numerous court decisions under the original act, clearly indicate that the act contemplated *sequestration rather than confiscation*. The amendment of March 28, 1918, however, broadened the powers of the Alien Property Custodian so as to include the right to manage or sell the property 'as though he were the absolute owner,' and in the so-called Chemical Foundation case¹ decided by the Supreme Court on October 11, 1926, the Supreme Court held that when any of the property was sold the former enemy owners were deprived of all rights in the property and in the proceeds derived from the sale. Though it was unnecessary for the purposes of this particular decision, the language of the court is broad enough to be open to the construction that the seizure of the property under the authority of the Trading with the Enemy Act, as amended, together with the applicable treaty provisions, deprived the owner of all rights, whether or not the property was sold, and that the property was virtually confiscated.

It is to be noted, however, that even if the property is held to have been confiscated, *in spite of the clear*

¹ *United States v. Chemical Foundation*, 272 U. S. 1.

intent of Congress to the contrary, Congress nevertheless has retained at all times absolute authority over this property and could at any time not only return it to the original owner but declare it to be held for the benefit of and for ultimate return to the original owner. . . . So that notwithstanding the undoubted power of Congress to confiscate, reaffirmed in the Chemical Foundation case, Congress not only has refused to exercise that power up to the present time, but has clearly by legislation asserted its policy to be the very contrary of confiscation."

A similar attitude on the Senate-side is found in the report by Senator Smoot for his Committee (Senate Report No. 273, 70th Congress, 1st Session), where he states at page 2:

" . . . Under the Knox-Porter peace resolution, which was incorporated in the treaty of Berlin, the United States unquestionably possesses the right to retain this property until Germany has made suitable provision for the satisfaction of the claims of American nationals against the German Government. Unless, however, Congress is prepared to adopt a policy of confiscating the property of an enemy national to pay the debts of his government some provision must be made for a more immediate return of this property."

Mr. Green said much to the same effect on the Floor of the House (Congressional Record, Vol. 68, Part 1, page 595):

"At the last session of Congress there were in general two propositions for the disposition and settlement of these claims. The first involved a virtual confiscation of the property which was in the hands of the Alien Property Custodian and its application to the payment of the American claims. . . . I am quite sure that a great majority of the House are against the confiscation of private property seized in time of war, and believe that such property should ultimately be returned."

The foregoing quotations (italics being our addition for emphasis) comprise statements by the members who had

charge of the bill on each Floor, and both men were in Congress when the Trading with the Enemy Act was enacted. Many similar repetitions might be added showing the views of Congress itself, that the seizures had not been made as confiscations, but as sequestrations, and that a subject under discussion during debate on the Bill was whether confiscation should then occur *for the first time*. The above quotations range from December 1926 to February 1928.

Not only are those quotations confirmations of the position expressed in our contracts, but also statements made contemporaneous with the Trading with the Enemy Act, express the same sentiment.

When the Trading with the Enemy Act was under consideration in committee, Secretary Redfield spoke before the committee on May 29, 1917 as follows:

"The creation of an alien property custodian is a novelty and is in line with that same effort toward equity which impels us to indicate an earnest desire to show to the people with whom, unfortunately, we are engaged in war that *here is the opposite of confiscation and here is the opposite of requisition.*" (Italics ours)

Again, on November 14, 1917, after the enactment of the Act on October 6, 1917, A. Mitchell Palmer, the Alien Property Custodian issued a statement through the Official Bulletin:

"The purposes of Congress are to preserve enemy owned property in the United States from loss and to prevent every use of it which may be hostile and detrimental to the United States. . . . The Alien Property Custodian exercises the *authority of a common-law trustee*; there is *no thought of a confiscation* or dissipation of *property thus held in trust.*" (Italic ours)

The report of the Committee on Commerce (Report No. 113, 65th Congress, 1st Session) on the Bill, stated:

" . . . Under the old rule warring nations did not respect the property rights of their enemies, but a more

enlightened opinion prevails at the present time, and it is now thought to be entirely proper to use the property of enemies *without confiscating it* . . . While the theory on which the bill is drafted is that enemy property shall be protected and utilized, *but not confiscated*, the ultimate disposition of the enemy property received and held by the Government is left to Congress, and provision is made that after the end of the war *enemy claims to such property* 'shall be settled as Congress shall direct.' " (Italics ours)

When Congress adopted Public Resolution No. 8 of July 9, 1921 that terminated the war, and which contained the provision to the effect that seized property would be retained "until such time as the Imperial German Government . . . shall have . . . made suitable provision for the satisfaction of all claims against said Government", Senator Knox, who had charge of the bill on the Floor stated (Cong. Rec. Vol. 61, Part 4, Page 3249):

"The purpose of the joint resolution is simply to hold in status quo the things that have been done by the Alien Property Custodian. The joint resolution simply states that until a suitable adjustment has been made of the claims of American citizens against Germany for the property that has been seized by Germany, the property in the hands of the Alien Property Custodian shall be held until Congress shall dispose of it . . . not that we are in any way committing ourselves to the proposition that we are going to retain alien enemy property, but that we are going to retain it only until suitable provision has been made for the satisfaction of American claims against Germany and against Austria."

By the Act of March 4, 1923, known as the Winslow Act, (42 Stat. 1511) provision was made for the return of property within certain limitations, and that Act also contained amendments to the Trading with the Enemy Act. A Section 23 was added to that Act, reading:

"The Alien Property Custodian is directed to pay to the person entitled thereto, from and after the time

this section takes effect, the net income, dividends, interest, annuity, or other earnings, accruing and collected thereafter, *on any property or money held in trust for such person* by the Alien Property Custodian or by the Treasurer of the United States for the account of the Alien Property Custodian. . . ." (Italics ours)

It thus is made evident that when we engaged upon a contract with the claimants for "the return of the Claimant's property" as being "now held in trust for the Claimant by the Alien Property Custodian" (R. 33), we had the same attitude in the matter as had been expressed prior by Congress and which continued to be expressed thereafter by Congress, regardless of the statement in the *Chemical Foundation* case and with which statement members of Congress themselves disagreed.

The very term "confiscation" when speaking as something to be done thereafter (as is true throughout the debates on the Settlement of War Claims Act), necessarily recognizes the existence of legal rights and property interests within somebody other than the one who contemplates the confiscation.

Reverting to the situation in 1917, we quote from the Hearings before the House-Committee on Interstate and Foreign Commerce, May 29, 1917:

"*Secretary Lansing*: The general purpose of the bill you have already stated, Mr. Chairman, that is, to stop commercial intercourse with the enemy. The basis of the bill is not, as it is in the case of the action that has been taken by the allied Governments, the nationality of the persons affected, but the domicile of the persons. We consider that the only trade that will materially aid Germany is that which reaches the German soil, and to prevent this is the purpose for which this bill is drawn. . . .

The balance of the act deals more particularly with its general application and how it will operate in the matter of continuing patents and the *sequestration* of enemy property in this country in order to carry out

the idea of complete non-intercourse with the enemy. (Italics added)

The Chairman: The letters that I have had on that subject criticize these provisions and charge something like confiscation. I have replied to all of them, stating that there is no such intent in the law, but merely to hold the property in doubtful cases, the whole thing to be adjusted after the war, and that there will be no final injury to anybody.

Secretary Lansing: Exactly. In fact, it is a protection, a very decided protection to the property owner, because enemy property is subject to seizure by act of Congress. . . ."

Over and over again, at the hearings on the bill, in the reports of Committees, and by statements in debate in House and Senate by members having the bill in charge, the statement was repeated,—that the bill intended sequestration as distinct from confiscation, that seizures contemplated protection to the owners as well as purposes related to the conduct of the war. Further quotations practically would mean a doubling of the contents by the entire Congressional Record, hearings, and Committee Reports, all of which clearly would evidence and would make more understandable the insistence by the members of the Congress dealing with the Settlement-Act, that confiscation was not intended by the Trading-Act,—regardless of the Chemical-Foundation decision.

The Settlement of War Claims Act comprised eleven sections by way of amendments to the Trading with the Enemy Act and nine sections by reason of inclusions relative to settlement of the claims of American-nationals and other matters relative to the compromise-agreement of the respective claimants on the two sides.

An Act of March 28, 1918 (40 Stat. L. 460) and an Act of November 4, 1918 (40 Stat. L. 1120) enlarged the powers of the Alien Property Custodian so as to authorize the sale of properties seized. Pursuant thereto, most of the seized properties were sold, the proceeds found investment

in bonds of our Government, and the final disposition of the "seized properties" by the Settlement-Act became a matter of a disposition relative to the converted properties in possession of the Alien Property Custodian in 1928.

Those converted properties (together with any original seizures that had not been sold) were accounted-for by the Custodian under the name of Trusts relative to the names of claimants. There were 16,000 such Trusts still active, in 1926 when the House Committee held its hearings. (See, testimony of Howard Sutherland, Alien Property Custodian, April 5, 1926, "Return of Alien Property," *supra*, pp. 71-103 therein).

The Settlement-Act dealt with the *properties within those Trusts*, limiting all claimants to the amounts therein, and barred any claim by them relative to a greater value being comprised within the properties as originally seized. The German-claimants accepted that solution of their claims (as the Settlement-Act provided) upon notifying the Custodian of their acceptance relative to the retention of 20 per cent of the amounts standing in their respective Trusts,—all as had been agreed to in the compromise-agreement signed by representatives of the two groups of the claimants. For the convenience of the Court we quote that agreement from page 129 of the Senate Hearings of January 13, 1927 (*supra*), directing attention to the admission of *ownership* relative to the Trusts as being in the German-nationals. The agreement provided:

"December 1, 1926.

Hon. William R. Green,
Chairman Ways and Means Committee,
House of Representatives.

Dear Mr. Green: For your information and that of your committee in drafting proposed legislation, we note the following as a general basis of agreement between the American and German interests which we respectively represent:

1. Twenty per cent of the alien property fund to be temporarily retained and so invested in Dawes plan an-

nunities as to become applicable to the immediate payment of American claims, the balance of the 80 per cent of the alien property fund to be promptly returned to the owners.

2. Fifty per cent of awards for payment of German ships, radio stations, patents, etc., to be likewise temporarily retained and applied to American claims as soon as it becomes available, and the balance of such awards distributed to ship owners, et al.

3. The \$26,000,000, approximately, of unallocated interest in the hands of the Treasury to be similarly applied to American claims.

4. The \$14,000,000, approximately, of Dawes plan payments received up to September, 1927, to be applied to the payment of American claims.

5. All funds in the hands of the Alien Property Custodian formerly belonging to the German Government, together with all funds so held the ownership of which is not disclosed within a period to be fixed in the bill, and thereafter established to be applied to the payment of American claims.

6. To the extent that the above payments on the American claims falls short of 80 per cent of the total amount of such claims, including interest thereon as awarded to January 1, 1927, the receipts from the Dawes plan payments accruing subsequent to September, 1927, to be first applied to payment thereof until such 80 per cent has been paid in full, and thereafter said receipts from the Dawes plan payments to be distributed ratably among the remaining unpaid claims of Americans, alien property claimants, and ship, radio, and patent claimants, together with $3\frac{1}{2}$ per cent interest thereon, until they are paid in full; and thereafter these Dawes plan payments to be applied as they accrue to the payment of the \$26,000,000 of unallocated interest advances as aforesaid, together with $3\frac{1}{2}$ per cent interest thereon until paid, thereafter the Dawes plan payments to be applied to the payment of the United States Government awards against Germany.

WILLIAM P. SIDLEY,

For the American Claimants.

W. KIESSELBACH,

For the German Claimants."

IV.

The Settlement of War Claims Act involved no element of "Favor Legislation," in distinction from "Debt Legislation."

The opinion of Judge Biggs (R. 45, 46) deems our contracts to have been *void*, for the asserted reason that they sought "favor legislation" instead of "debt legislation", thus implying a validity to the contracts if they had sought "debt legislation". He admitted that he obtained that view from the decision of the Court of Appeals for the District of Columbia, in the case of *Brown v. Gesellschaft Fur Drahtlose Telegraphie M. B. H.*, 104 Fed. (2d) 227.

That case involved an attempt by a lawyer (who previously held connection with the office of the Alien Property Custodian) to recover his fees under a contract with one of the German nationals for the lawyer's services in connection with the Settlement Act. Under those facts, the court deemed the contract to be contrary to public policy and denied a recovery. (See first appeal of the case, reported in 78 Fed. (2d) 410.) The court might have quoted that passage in the Bible which declares that "no man can serve two masters", and have rested the decision upon that Authority. But, the court engaged upon *obiter dicta*, declaring that the German nationals never possessed any "lawful existing claim", sought "favor legislation", and therefore the contract was void anyway.

The petitioner cannot stand prejudiced by that *obiter dicta* through any failure by Brown's counsel properly to inform that court regarding the Settlement Act and the Trading Act, as we have endeavored to do in the foregoing subdivisions of our argument.

The utilization of the *Brown* decision conveys the implication that if the Settlement Act involved "debt legislation" the expenses quite properly would have been deductible; but, involving "favor legislation", they were not deductible.

Regarding the views of his colleague, Judge Maris stated (R. 67, 68):

“I have grave doubt of the soundness of the distinction thus drawn between ‘favor legislation’ and ‘debt legislation’ . . . The distinction sought to be drawn, as I understand it, is between legislation designed to provide for or facilitate the settlement of existing claims against the government and legislation which confers benefits upon individuals who had no claims against the government prior to its passage. This distinction seems to have been first expressed by the Court of Appeals of the District of Columbia in the first Brown case, *supra*. I do not find the distinction referred to in any decision of the Supreme Court of the United States. On the contrary the rule of that court seems to be to strike down such contracts as against public policy if it appears to the court that they are likely to facilitate and encourage the corruption of the legislative body. *Trist v. Child*, 88 U. S. 441. If this is the test, as I think it is, it would seem to follow that “debt legislation”, since it is ordinarily devoid of general public interest and, therefore, not subject to public scrutiny during the process of enactment, would provide a much greater opportunity for legislation corruption than ‘favor legislation’ which ordinarily affects a larger section of the public and is, therefore, subject to much greater public attention while being considered by the legislative body . . . I am clear that in any event the validity of the contract has no bearing on the question before us, for reasons which will be discussed later. But even if its bearing be conceded it seems to me that the Settlement of War Claims Act was in fact “debt legislation”.

We add to that clear analysis by Judge Maris with a question:—What is the difference between appealing to Congress for a “favor” of legislation, and appealing to Congress to appropriate money for the payment of a “debt”,—as a favor?

People who possess *legal rights*, never have to seek an Act of Congress. They seek the desired result through the judicial processes.

It is only when they *lack* enforceable rights, that they seek the remedy from Congress. We make the bold assertion,—that there *never* is an Act of Congress which is *not* a favor, when special or specific.

"A favor is a benefit or kindness that one is glad to receive, but can not demand or claim, hence always indicating good-will or regard on the part of the person by whom it is conferred."

Funk & Wagnalls Standard Dictionary.

The "favor" element exists in every kind and description of special Act enacted by Congress. There is no exception whatsoever. Every time that Congress so expresses itself by legislation, *it is a favor*. What of it, if persons hold appointive offices? They cannot receive compensation, except as Congress acts by an appropriation measure. Nobody can compel Congress to do so. The payment of a "debt" is just as much a "favor", by the grace or blessing of Congress, as legislation which creates any appointive office or authorizes the appointment. The Sovereign cannot be compelled; its favor may be sought; every Act is a "favor".

We illustrate by the famous "French Spoliation Cases". The "debts" (if we grasp the court's distinction in the *Brown* case) were established by Court of Claims decisions decades ago. The obligations were recognized by our Government in the Treaty with France more than a century ago. Generation after generation of descendants of the original owners who were damaged, have passed into the Great Unknown. President after President (also now passed into that Great Unknown) has recommended to Congress that the "debts" be paid by enactment of the proper appropriation bills. The present generation of descendants still await the "favor/legislation" that will pay those "debts". Congress, in 1885, instructed the Court of Claims to make the monetary determinations; that court rendered judgments from 1905 to 1916 totaling more than three million dollars,—which still stand unsatisfied. Mindful of that history and the fact that attorneys only can find compensation upon a contingent basis, it would appear far more difficult to obtain the "favor" of Congress for "debt legislation" (with the objections mentioned by Judge Maris) than for "favor legislation".

The Settlement Act was a matter of bestowing "favours" by all parties concerned: By the compromise agreement each side "favored" the other, and both "favored" the Members of Congress who frankly admitted by Committee report that the problem never could have been solved, except by the compromise;—and Congress "favored" everybody by enacting the agreement into an Act.

We do not question in the slightest degree, but that the Act was a "favor" from Congress,—by the very same token that *every* Act is a favor relative to the particular persons who gain benefits. (See, *Cummings v. Deutsche Bank*, 300 U. S. 115.)

The Act was a "favor" to the American claimants in a sense equal to the "favor" bestowed upon the German claimants.

The possession of a *claim* is quite different from a *legally enforceable claim*. As to the latter, no legislation is needed.

"The term 'claim' is of course ambiguous, but it would seem that while the German interests had no 'property' in the confiscated items, they certainly had some moral ground for reimbursement." (Note on case below, *Chicago Law Rev.* Vol. 8, 779)

"Adopting the norm of the judicially ideal business man by disallowing deductions wherever the enterprise does not meet some vague standard of public policy is an unwarranted change by judicial decision in the concept of taxable income. In addition, it burdens the courts, in construing taxing statutes, with all the archaic definitions of public policy evolved in contract law. Cf. *Helvering v. Hallock*, 309 U. S. 106." (Note on case below, 54 *Harvard Law Rev.* 699)

"Favor legislation" might be deemed as a grant by a Sovereign through legislative action, in a situation where there was no semblance of a claim, no reasonable basis for asserting a claim, no excuse whatsoever for alleging damage or loss if the legislation were denied.

Where, however, a person has made investment in a foreign country and is deprived of that property by a Sover-

eign action, it is beyond comprehension that he has no right to ask that Sovereign to make a restitution. Such a right, when addressed to the Sovereign, is a *claim*, even though the decision may rest with the Sovereign's discretion or free will, as distinct from a legally enforceable right. From the time of seizure in Germany, our citizens possessed a claim *against Germany*; equally, the Germans had a claim against us, for the seizure of their property.

The very Act that authorized the seizure recognized that claims would be created with the seizures. The Joint Resolution of July 2, 1921 recognized the existence of claims, by the very language that insisted upon a *retention* until "suitable provision" was made by Germany for the seizure of the properties of our citizens. The Settlement Act recognized *the existence of claims*, because its whole purpose was,—*the settlement of claims*.

We assert, therefore, that the decision in the *Brown* case, *supra*, and the opinion by Judge Biggs in the court below, were predicated in error upon the non-existence of claims. Should it not suffice that Congress itself recognized the representatives of the two groups of "claimants" and enacted into law *their compromise agreement*?

The First Amendment to the Constitution declares:

"Congress shall make no law respecting . . . the right of the people . . . to petition the Government for a redress of grievances."

There are certain matters where a direct contact (and expenses) as between private persons and members of Congress is permissible and essential. The American claimants had "grievances" and the German claimants had their "grievances", but the foreigners necessarily had to present their "grievances" through representatives in the United States. What the Commissioner sees fit to call "legislation" (when applying the Article 262 of Regulations 74) and the court in the *Brown* case, *supra*, calls "legislation", (the opinion by Judge Biggs as well) was nothing but a Congressional approval for a settlement of the grievances

in terms of a compromise agreement as between the respective petitioners who had presented their grievances,—to Congress, as their Constitutional right. In a truer sense, the Settlement Act was *special legislation*, more fittingly to be described as *quasi-judicial* because it merely approved the settlement agreement between the two groups of aggrieved claimants.

Special legislation, inevitably, must *favor* the persons for whose special benefit the Act is enacted. Those persons alone can advocate the enactment, and they alone can contact the members of the legislative body.

Principles of law which might be applicable, on grounds of public policy, to matters of *general* legislation involving the public interest as distinguished from the interest of particular groups, have no application, we submit, to the situation in this case,—of such peculiar facts in relation to *special* legislation.

V.

The fact of contingent contracts did not make those contracts void or illegal, as being against public policy.

Under Part I of our Argument, we explained the necessities for contingent contracts in this matter. The Germans had no other means for compensating us, except relative to what they might recover from the properties in possession of the Alien Property Custodian,—if the legislation resulted.

Contingent contracts may be an *unfortunate necessity* (from the agent's viewpoint) but they are not "sinister" *ipso facto* and without opportunity for an explanation. "Improper influence" may just as easily be exerted through substantial flat payments in advance of the services to be rendered, as under contingent contract arrangements. If the principal and agent are dishonest, unconscionable, unethical, and criminal-minded, the advance payments easily may exceed proper compensation for the services and contemplate by such excess an improper use of the money. The

mere *form* of contract cannot be a guaranty as to honorable conduct. Such conduct comes from the *soul*, not from the pocketbook.

In *Steele v. Drammond*, 275 U. S. 199, this Court stated (when holding that the contract there involved was not void as against public policy):

“ ‘All persons whose interests may in any way be affected by any public or private act of the legislature have an undoubted right to urge their claims and arguments, either in person or by counsel professing to act for them, before legislative committees, as well as in courts of justice.’ While the principle is readily understood, its right application is often a matter of much delicacy. It is only because of the dominant public interest that one, who has had the benefit of performance by the other party, is permitted to avoid his own obligation on the plea that the agreement is illegal. And it is a matter of great public concern that freedom of contract be not lightly interfered with. . . . The meaning of the phrase ‘public policy’ is vague and variable; there are no fixed rules by which to determine what it is. It has never been defined by the courts, but has been left loose and free of definition, in the same manner as fraud. . . . It is only in clear cases that contracts will be held void. The principle must be cautiously applied to guard against confusion and injustice. . . . Detriment to the public interest will not be presumed where nothing sinister or improper is done or contemplated.” (Decision unanimous; omissions represent citations)

In *Valdes v. Larrinaga*, 233 U. S. 705, a unanimous court held the contract there involved (which, incidently, made compensation contingent upon the result), not void as against public policy, Mr. Justice Holmes stating, in part:

“ ‘But we discover nothing in the language of the letters that necessarily imports, or even persuasively suggests, any improper intent or dangerous tendency.’ ”

In *Spalding v. Mason*, 161 U. S. 375, a contract for sharing fees under some 7,500 claims that were established by

an Act of Congress through the services of an attorney upon a contingent basis, was enforced by this Court.

In *Winton v. Amos*, 255 U. S. 373, recovery was recognized on a *quantum meruit* basis for services in procuring an Act of Congress beneficial to Indians, although the written contracts with the Indians were invalid by reason of their lack of power to contract. The Court stated, in part, at page 393:

"We have no doubt that, for proper professional services in promoting legislation that has for its object and effect the rescue of substantial property interests for a class of beneficiaries under a trust of a public nature, it is equitable to impose a charge for reimbursement and compensation upon the interests of those beneficiaries who receive the benefit, the same as if a like result had been reached through successful litigation in the courts."

In *Nutt v. Knut*, 200 U. S. 12, a contingent contract for the procurement of an Act of Congress was enforced as not contrary to public policy.

The decision in *Steel v. Drummond*, *supra*, more recently has found approval by this Court in *Twin City Pipe Line Co. v. Harding Glass Co.*, 283 U. S. 353, at 356, 357; and *A. C. Frost & Co. v. Coeur D'Alene Mines Corp.*, 312 U. S. 38; 85 Law. Ed. 383, at 387 (See, Note on that case, 50 Yale Law Journal 1108).

The court, in the *Brown* case, *supra*, makes no mention of the case of *Steel v. Drummond*, *supra*.

In the court-below (R. 46) the attempt was made by one of the adverse opinions to distinguish the case of *Steel v. Drummond*, *supra*, from the case at bar, for the reason that Drummond had a "property interest" in the matter of legislation, separate from his contract obligation. It is impossible for us to perceive how there could be less of a tendency for "improper influence" in a situation where a man held the additional interest of ownership-plus-contract, than where he held a contract-obligation *without* an ownership.

It seems to us, rather, that such decisions as hold for a violation of the public policy rule, tend more to resemble such situations as shown in the recent case of *Ewing v. National Airport Corp.*, 115 Fed. (2d) 859,—relative to which this Court denied Certiorari on March 31, 1941. The contract there involved, expressly contemplated the use of political influence in obtaining legislation from Congress upon a contingent fee basis, and was performed by promising members of Congress his political help in their election districts, in return for their support by voting for his Bill. The court stated:

“ . . . no court will lend its assistance in anyway toward carrying out the terms of an illegal contract; that a contract to secure the passage of legislation by any other means than the use of reason and presentation of facts, making arguments and submitting them orally or in writing, is invalid as a ‘lobbying contract’.”

The situation in that case was much the same as in the leading case of *Trist v. Child*, 21 Wall. 441, relative to the kinds of contracts which *will or will not* be enforced. Both were instances of personal solicitation of legislators, with a complete absence of an appeal to reason or fair-argument, and with an exertion of improper influence.

On the general subject, we refer to Restatement of the Law, 17 Corpus Juris Secundum, “Contracts”, Section 213.

We suggest application to the facts of the case at bar, of the statement in *Trist v. Child*, *supra*, regarding *enforceable* contracts:

“We entertain no doubt that in such cases, as under all other circumstances, an agreement express or implied for purely professional services is valid. Within this category are included: drafting the petition to set forth the claim, attending to the taking of testimony, collecting facts, preparing arguments, and submitting them orally or in writing, to a committee or other proper authority, and other services of like character. All these things are intended to reach only the reason of those sought to be influenced. They rest on

the same principle of ethics as professional services rendered in a court of justice, and are no more exceptionable."

We agree also with the high standard of morality, as set forth in the opinion of Mr. Justice Swayne (pp. 451, 452) in that case.

We submit the Record as showing that our conduct met every requirement of the standard.

A very clear evidence either of carelessness or plain oversight, is submerged in the adverse opinions of the court below. That comes to light in the opinion of Judge Clark by way of a dissent in the case of *Girard Trust Company v. Commissioner*, 121 Fed. (2) . . . , decided in the Third Circuit on June 27, 1941, where he describes the case of *this petitioner* as:

"the secret influence type".

The Exhibits B and C were presented to Congress by us,—one being accepted and printed as a Senate Document, the other being presented to the Ways and Means Committee by our own attorney and printed as part of the hearings by the Committee itself. What was "secret" about it? Both in the Senate and the Committee, if any Member of Congress considered that *who paid for the work* evidenced in those documents, was of the slightest importance, questions could have been asked and they would have been answered. The very fact that the documents presented data *against confiscation*, showed clearly enough that the American-claimants (who were seeking confiscation) had nothing to do with those documents, and there was only one other interested party, namely,—those who opposed confiscation, the German-claimants.

It equally is true of the work of "Ivy Lee", in the campaign of education. Should American newspapers and magazines accept and print *only* the advocacy of the *American-claimants for confiscation*? Should the American people be kept in complete ignorance with regard to the continuous

policy of our Nation back to the time of the Revolution for our independence, when the *Tories* were compensated for the seizure of their property during that war? Should they be kept ignorant of the fact that the same policy had continued throughout every other war? Should they be kept ignorant of provisions in treaties that had recognized that same policy? In such ignorance, should they "write your congressman urging confiscation", in response to the plea by the American-claimants? Should the congressmen, overwhelmed by such ignorant insistence from constituents, be forced to express that ignorance, without their own free will? Were not the congressmen entitled to know the truth, as to our policy, so that they might set their constituents into the paths of truth?

Work along those lines relative to the expenses here in question, is *all that we did*. The work was educational, but it had nothing whatsoever to do with "the secret influence type".

Upon the completion of that education regarding our past policy, it became a matter solely for the *free choice of Congress*, either to maintain that policy or to break the chain, and to order confiscation.

That confiscation would have been a bad policy, needs little comment. No foreigner thereafter would invest in the United States and the investment of our citizens in foreign countries would have had no assurance for safety. What we had done, they could do,—confiscate.

VI.

An unenforceable contract is not illegal in a sense of being criminal.

The principle that contracts in contravention of public policy will not be enforced through judicial processes, is based upon the maxims, *Ex dolo malo non oritur actio*, and *In pari delicto potior est conditio defendentis*.

As expressed in *Trist v. Child, supra*; "Where there is turpitude, the law will help neither party."

Where such contracts have been *executed*, the fact of "illegality" cannot cause a utilization of the courts for a restitution. It is a two-edged sword that denies judicial redress completely. (See, Restatement of the Law, 17 Corpus Juris Secundum, "Contracts", Section 272 et seq.)

Yet, the opinions in this case by Judges Biggs and Clark (R. 42-66) dealt with a matter of *unenforceability*, in terms of the equivalent of *malum prohibitum* or a violation of positive statutes—and thus, criminal in nature. (Or was it *malum per se*?)

A disallowance of a deduction in the ascertainment of taxable income by predication upon the unenforceability of a contract, would carry into such extreme confusion as to merit the most careful consideration by this Court. The identical language of a contract may be deemed enforceable in one State, but unenforceable in another. In one State the business may be "legal", in another "illegal". The decisions in various States are so variant with regard to the dictates of "public policy" as to provide no norm for reason and action.

We can state that phase of this case no better than by quoting from 8 Chicago Law Review, at 778, with relation to Note on the decision by the court-below in the case at bar:

"Also, in the instant case, it was said that the deduction could not be allowed because the expenditure was made in pursuance of a contract which was itself contrary to public policy . . . Not only may the use of this argument be criticized on the ground that refusal of the deduction is not a proper means of enforcing the policy, but it may also be objected to because it is not at all clear that the contract was against public policy. If, under *Eric v. Tompkins*, state law is applicable . . . the federal courts are faced with a variety of state decisions, . . . some of them holding that contingent fee contracts for lobbying are void, . . . others holding that the contracts are valid unless there is proof that improper acts were actually contemplated or done . . . Under the federal decisions, there is an equal lack of uniformity . . . Usually, where there has been personal contact with individual legislators, the contract is held void. Yet in one case the court allowed quasi-contractual relief to lobbyists for the Choctaw Indians in spite

of the fact that the claimants engaged in all types of lobbying activity, including personal solicitation . . . If personal solicitation does not render the contract void, it would seem that, a fortiori, a contract for the type of activity involved in the instant case would be enforceable." (Citations omitted)

Equally pertinent to this phase of the discussion is the Note relative to the decision by the court-below in the case at bar, in 54 Harvard Law Review, at 859, 860:

"... justification of disallowances on grounds of effectuating public policy must overcome both the contrary import of the statutory language . . . and the countervailing policy against judicial conversion of a tax on net income into a possibly exorbitant tax on gross receipts . . . In addition, the extension from the concept of illegality arising from criminal and regulatory statutes to the concept of effectuation of public policy involves the acceptance en masse of all the artificiality such a vague standard must necessarily contain . . . The negligible relation of such a standard to the determination of what the tax burden of an individual taxpayer should be indicates that even though the restricted concept of illegality be retained, the broad concept of effectuating public policy should be discarded. To do so will, of course, result in the loss of haphazard additions to the national revenue. But increases in revenue should come either from an extension of tax liability or from an increase in rates, rather than from the distortion of a relatively rational system of taxation." (Citations omitted)

An examination of decisions in various States regarding public policy, makes evident that some jurisdictions hold so little confidence in the ability of their legislators to withstand or repulse "improper influence", that the courts feel compelled to enfold the legislators within a protecting mantle; other jurisdictions express a greater degree of confidence in the integrity of their legislators, or their ability *not* to be improperly influenced, that more lenient standards are expressed relative to "public policy".

Projecting such divergent views onto the "screen" to picture Taxation, can add chaos to an already existing confusion.

VII.

The determination of net income in an illegal business should be by the same standards as for a legal business.

The position of the Commissioner and of the two adverse opinions is that illegal businesses should be taxed upon their gross receipts as "net income." Presumably, that position finds interpretation of the revenue acts into a meaning by Congress that the deduction for expenses applies only to carrying on a "legal" business.

The revenue acts always have said "in carrying on *any trade or business*." Now, it is advanced, the language should be changed (without an Act of Congress) into "any *legal* trade or business."

For the twenty-eight years of interpretation by Regulations, no such interpretation ever has been made. Not even can "the reenactment rule" find an invocation. (It is hoped that we will not now be troubled by a new creation as, "the non-enactment rule.")

We have not been able to locate any precedent for the proposition that in an illegal business the "net income" is the gross receipts.

Nor (except for the case at bar) can we find any case where the Commissioner has urged the contention—unless *Steinberg v. United States*, 14 Fed. (2d) 564, represents such an attempt, with a repudiation of the doctrine by the Second Circuit.¹

United States v. Sullivan, 274 U. S. 259, involved an instance where this Court held that taxation could not be evaded by an argument that the business was illegal. This Court did not rule upon the question how the taxable net income should be determined. In the opinion, this Court said:

¹ See, however, varying aspects of the matter in, *Alexandria Gravel Co. Inc. v. Commissioner*, 95 Fed. 2d 615; *Sullivan v. United States*, 15 Fed. 2d 809; *Helvering v. Hampton*, 79 Fed. 2d 358; *McKenna v. Commissioner*, 1 B. T. A. 326; *Frey v. Commissioner*, 7 B. T. A. 338; *Terrell v. Commissioner*, 7 B. T. A. 773; also, *Bureau Ruling, IT 2175*, Cum. Bul. IV-1-141; and *Bureau Ruling, S.M. 4078*, Cum. Bul. V-1-226 (cited with approval in *Kornhauser v. United States*, 276 U. S. 145, 153).

"It is urged that if a return were made the defendant would be entitled to deduct illegal expenses such as bribery. This by no means follows but it will be time enough to consider the question when a taxpayer has the temerity to raise it."

We understand that this Court meant that if any taxpayer desires to admit the commission of a *second* crime, and claim as deduction the expenses of that other crime as against receipts from the commission of the *first* crime, "it will be time enough to consider the question" when such an admission is made to the Court. In other words, the case itself did not involve the ascertainment of liability for taxes (it was a criminal prosecution for failure to file a return); if a proper case were presented, the Court would consider the contentions—"temerity," because a different crime thus would have to be admitted, opening the culprit to another criminal prosecution under state laws.

There are instances where a taxpayer is engaged upon a certain business which could be conducted without the commission of any crime, but laws are violated, prosecutions result, and money is expended in defense (unsuccessfully). Such expense is not deductible, *because crime was not the business*. Without doubt, such cases as *Burroughs Building Material Co. v. Commissioner*, 47 Fed. (2d) 178, (which apply to that exact situation) will be cited by the Government in this case.

For the convenience of this Court, we refer to a complete citation of all such decisions, with comments relative thereto, in Note, 54 Harvard Law Review 852. For the reason that the analysis by that Note is so complete, our reference thereto avoids a repetition of discussion in this brief.

It impresses us that the question has far greater importance relative to a reasonable application of tax laws, than relative to "catching" somebody with taxes by a technicality. When the Government requires revenue, it is a most simple process to produce the result by increases in rates. (The rates under existing revenue laws are more than *double*, by comparison with rates during the First World War.)

If such a doctrine found encouragement as "violation of law deprives of deductions," the tax controversies would find increase by the tens of thousands (a most conservative estimate).

In our vast country there are countless numbers of people who gain their livelihood "by taking chances." In a sense, all business undertakings are "chances," and the professional gambler deems that he is just as much "in business" as "the other fellow." Without it, he would starve.

Among our forty-eight states there are varying views pertaining to what is, or is not, a lawful business. Liquor can be sold in some states, not in others. Cigarettes can be sold in most states, not in some. Betting on horse racing (and dog racing) is legal in some states, not in others.

Selling this and that is legal in some states, illegal in others. Operating theatres is controlled in various states in different ways, making for one thing as legal, another as illegal. Wages and hours acts, employment of women after certain hours, child labor, sanitary or health provisions, operating a business in violation of the rights of others relative to patents, trademarks, trade names, or unfair methods of competition, operating without a license under supervised situations relative to police powers, even operating hotels in certain states in violation of statutes relative to the length of beds, the length of sheets, or the number of blankets may violate state laws; charging a prohibited rate of interest on loans, and so on *ad infinitum*; there is no limit to the possibilities relative to operations of *business* in violation of law—*mala prohibita*, not merely against an uncertain "public policy."

When one engages upon the problem of determining the deductibility of an expense by the validity of the business operation, it would not be a matter of ascertaining the "net income" in terms of "gains, profit, or income"; it would be a matter of taxing the *gross receipts* as a penalty for a violation of some state law in a major or minor respect. It would not find excuse by the "ability to pay" doctrine. Let us picture a race track gambler "following the horses"

from Santa Anita to Saratoga, betting wherever he goes, regardless of state laws, pari mutuels, or otherwise. He pays for "tips"; he pays his traveling expenses—all in a hope for gain in the *only* business that he has. By his gains he lives, he profits, or he loses. As he travels, his bets may be legal in one state, illegal in another. From the Federal aspect, what is his "ability to pay taxes," to share the burden of our Government? Must we differentiate his operations between those states where betting is legal and those where it is illegal? Let us picture a manufacturer of liquor, shipping the product into one state where the sale is legal, into another where it is illegal. Does he have *greater* "ability to pay taxes" because of the illegal sales and a non-deductibility as to expenses proportionate thereto?

Equally, it might be said that it is not "ordinary and necessary" for a business to operate in violation of the Wages and Hours Act, employing women at night, child labor, and by disregard of numerous other restrictions. But, is the "ability to pay" taxes *increased* by denial of deductions relative to the illegal operations?

Gambling establishments may be licensed in one state, not in another. By the invocation of such a doctrine, one would be taxed on "net income," the other on gross receipts (theorized into being "income, gains, or profits"). Houses of prostitution are licensed in some states, not in others.

A licensed status might fail for nonperformance of a specified condition. The *state* does not prosecute, but some revenue agent makes his private investigation and "finds" the operation to have been illegal.

If any such doctrine applied, *every situation of taxes* would involve an ascertainment whether, here or there, some Federal law, state law, city ordinance, or license had been violated in the course of the business operation. Every tax case would be converted into a criminal prosecution.

That the matter already has reached enough of a state of confusion, see Note, 54 Harvard Law Review 852-860.

We refer also to Comments by Judge Maris (R. 70) where he opens his analysis by saying:

"It seems to me that the majority by this decision are converting into a penal statute what was intended by Congress to be solely a revenue measure."

But, it does *more* than that. It permits the Federal Government to exact a penalty for violation of some *state* law, city ordinance, or license, even though no prosecution occurred in the state or municipality. We thought we were progressing out of such realms by the decision in *Erie Railroad v. Tompkins*, 304 U. S. 64.

Our foregoing discussion relates to *malum prohibitum*—enough of a task in itself for prosecuting officials, without embarking revenue agents into that field.

The case at bar, however, as alleging to involve contracts "void because against public policy" injects us more into the field of *malum per se*, or the Common Law.

With states holding such contrary views regarding "public policy," we anticipate the bewilderment of revenue agents, attempting to ascertain taxes relative to how some state court *should* determine the "public policy" of that state as a means for the Federal Government to collect *penalties*.

VIII.

General Comments Regarding Ordinary and Necessary Expenses.

When expressing the unanimous opinion of this Court in *Welch v. Helvering*, 290 U. S. 111, Mr. Justice Cardozo described the term "ordinary" as (pages 113, 114):

"a variable affected by time and place and circumstances."

Later in the opinion in that case he stated (pages 114, 115):

"Here, indeed, as so often in other branches of the law, the decisive distinctions are those of degree and

not of kind. One struggles in vain for any verbal formula that will supply a ready touchstone. The standard set up by the statute is not a rule of law; it is rather a way of life. Life, in all its fullness must supply the answer to the riddle."

Mr. Justice Holmes stated the general subject-matter in *Schenck v. United States*, 249 U. S. 47, 52:

"the character of every act depends upon the circumstances in which it is done."

Again, did he state in *Towne v. Eisner*, 245 U. S. 418, 425:

"A word is not a crystal, transparent and unchanged, it is the skin of a living thought and may vary greatly in color and content according to the circumstances and the time in which it is used."

The same thought was expressed in *Deputy v. du Pont*,¹ 308 U. S. 488, 495, 496, by Mr. Justice Douglas:

"the fact that a particular expense would be an ordinary or common one in the course of one business and so deductible under Section 23(a) does not necessarily make it such in connection with another business . . . One of the extremely relevant circumstances is the nature and scope of the particular business out of which the expense in question accrued."

Applicable to the case at bar, it was both "ordinary and necessary" in the business upon which we were engaged by contracts, to protect the interests of our principals by preventing the confiscation of the property and its use in payment of the American-claimants. We were entitled to do so by every fair form of an appeal to reason, directly to Members of Congress and indirectly to them through their constituents. We were entitled to present the side of the German-nationals, who had expressed faith and confidence in our country by investing here. Their only argument was a *plea*, through us as their representative. We

¹ See, Annotations to that case in 85 Lawyers Ed. 416, at 426.

were fully aware that Congress *could* order a confiscation. The decisive question was, whether Congress *desired* to do so if informed that the policy of the United States throughout our entire history had been consistent against confiscation of enemy property. How would Congress and the American constituents *know* of that policy, unless somebody collected the data? Who could or would collect it and print it and distribute it, except the representatives of those German-claimants? Clearly, the *American*-claimants would not do so; their only interest was in the payment of their claims. We had to do it, and to bear the expense.

The material which we supplied was in every sense fair and was historically accurate. We were assisting Congress to a correct decision, in a sense equal to assisting our principals.

When the performance of contracts *is the business*, it is ordinary, usual, or customary for that business to perform the contracts, and to incur expense in such performance.

Not only was the "necessity" a fact, but also the Commissioner admitted the necessity for the expense by the Stipulation.

One of the adverse opinions in the court-below, at R. 47, 48, enunciates such an unusual and original theory, without citation of any precedent in support thereof, that we comment only briefly.

The idea is advanced for the first time in the history of income-taxation, that an expense is not "necessary" unless a taxpayer proves that the expense caused the result that was intended by the expense. Applicable to the Settlement Act, it is stated that the expense was not "necessary" unless we proved that the Act resulted because of the expense.

Previous to that statement, the interpretation of "necessary" always has been in the sense of "helpful", rather than by proximate causation. Obviously, if it were essential to establish the deduction by "proximate cause", there never could be such proof and the language of deduction

would be an absolute nullity. How can a merchant or a manufacturer *prove* that expense for advertising, repairs, salaries, wages, or for anything else, was the "proximate cause" of the gross receipts?

We submit the comments by Judge Maris (R. 71, 72) as disposing of the idea convincingly.

The Committee Report of Chairman Green and his statements to the House (both *supra*) shows that "the proximate cause" of the legislation was the compromise-agreement signed or approved by the two respective groups of claimants. But, what was "the proximate cause" of the *agreement*? Very obviously, when the American-claimants perceived that Congress did not favor confiscation, a compromise became possible.

The expenses in question were *an element* in the process of reaching "the proximate cause" of the legislation. As such an element, they were both "ordinary and necessary",—and the Commissioner so agreed when the case stood within the jurisdiction of the Board of Tax Appeals.

We approve and adopt as part of our argument in this regard, the analysis and reasoning by Judge Maris, Record 68 to 72 inclusive, which we quote in part;

"Section 7 of the Trading with the Enemy Act . . . clearly contemplated that the former owners had claims which would have to be dealt with after the war Here was not only the recognition of the existence of claims on the part of the former owners of seized property but also a clearly implied invitation to them to solicit from Congress legislation providing for the settlement of their claims Even though the taxpayer's contract was void . . . it does not follow that the expenses paid in carrying out the agency constituted by the contract were not ordinary business expenses. The illegality suggested is as to the manner of compensation and not as to the result sought to be accomplished The fact remains that the business contemplated by the contract was carried through, the contingent compensation was paid and is now being taxed, and the expenditures here sought to be deducted were expended in carrying on that business and earning that compensa-

tion. The alleged invalidity of the contract obviously does not affect the taxability of the income and I see no basis for holding that it affects the deductibility of the expenses

. . . . It is wholly beside the point to consider whether such expenditures would be ordinary in business generally. It is doubtless true that expenditures for lobbying activities were not ordinary in the case of persons engaged in mining, manufacturing or commercial business, but here lobbying was not merely incidental to the taxpayer's business but itself constituted the business. . . .

. . . . The majority have placed the stamp of illegality upon conduct which Congress has never declared to be criminal. I think that in thus restricting the plain language of the act this court is exercising a legislative and not a judicial function. I cannot agree that we have such power"

Regarding the closing part quoted above, we again refer to "The Struggle for Judicial Supremacy", *supra*, and the criticisms of courts for invading the field of legislation.

ARGUMENT

Part 3. The Court En Banc

ARGUMENT.

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The opinion of Judge Biggs (R. 50-58) argues the affirmative of the question. For the assistance of this Court on such a new matter that previously has not been considered by this Court, we adopt the negative side of the argument.

Relative to the particular case at bar, we direct attention to the opinion-below (R. 58);

“ . . . Where, however, there is a difference in view among the judges upon a question of fundamental importance, and especially in a case where two of the three judges sitting in a case may have a view contrary to that of the other three judges of the court, it is advisable that the whole court have the opportunity, if it thinks necessary, to hear and decide the question . . . ”

When this case was argued before the court of five judges, counsel was not informed that three of the judges desired to reverse the Board upon issues that were not presented to the Board, and that two judges felt that the case should be decided on the issue that *was* presented and decided by the Board. There was no suggestion that we argue the new issues.

We assumed, innocently and properly, that “the important question” related to the construction and effect of the Regulation, justifying consideration by five judges instead of the statutory three judges, so as to prevent possibly conflicting decisions in the future for that Circuit with regard to that question,—namely, the application of “the reenactment rule.”

Three out of the five judges did agree with the Board on that issue. Our confidence in the soundness of the Board decision thus was sustained, as evidencing why we raised no objection to five judges instead of three. But, relative to the original court of three judges (Biggs, Clark, and Maris) the majority of two (Biggs and Clark) just as easily could have decided *on those new issues* (disregarding the

issue in the Board and the facts found by the Board), without the addition of Judge Jones, to the side of Judges Biggs and Clark, and of Judge Goodrich, to the side of Judge Maris.

It might have been more embarrassing to have separate opinions by each of the *three* judges, one judge agreeing with the other two respectively, as to the issue before the Board (in one instance) and as to the new issues (in the other instance). In that situation, it might have been more difficult to order a Judgment of Reversal. The addition of one judge on each side made that result easier,—by a five judge court with two judges only concurring as to *two* out of the three opinions.

With that record before us *in the first case* that raises the question of the validity of a court *en banc*, we list objections to that procedure (not intending by a numerical order to stress the relative importance of the objections).

1. Just as Congress by the Act of 1925 relieved the Supreme Court from the burden of considering cases, by the abolishment of direct appeals in most cases and confining cases to the discretion of this Court through the grant of Writs of Certiorari, Congress in the future (controlled by a different political party) could “relieve” this Court by confining the jurisdiction to constitutional questions (or otherwise), thus making most decisions by circuit courts of appeal final and conclusive. Just as the number of circuit judges has been increased by various Acts in the past, so they could be further increased in order to supply majorities in each circuit that would reduce the present incumbents into position of ineffective minorities (through courts *en banc*). We thus would experience a *true* “court packing plan,” for reasons which it would be difficult, if not impossible, to refute. With the constitutionality of the Act of 1925 unquestioned, there is practically no limit to legislation for additional “relief” for this Court.

2. By the various Acts of Congress the appointment of additional judges has been authorized for respective cir-

cuits, on the ground that "the court" must sit as *three* judges, and that the volume of work required additional judges so that, by sitting in rotation, courts of *three* judges could keep the dockets more current. If all the judges of a circuit consider cases as courts *en banc*, either there are too many judges in that circuit or their ability to perform their duties in three-judges courts will be hampered. If four, five, six, and seven judges are called on to do the work of *three* judges, Congress readily can perceive that "there's something wrong in the State of Denmark." The most obvious answer will be, either to transfer them elsewhere to a circuit or district court where the docket is congested, or to abolish "the excess baggage."

3. The validation of courts *en banc* means, as a practical matter, that every judge will have to concern himself *with every case*, either before a hearing by a three-judges court or after such hearing by a three-judges court in which he did not participate. The greater the number of appointed-judges in a circuit, in that degree is the necessity for such scrutiny increased. View the circuits of *seven* judges; the four who do not sit on a three-judges court are the majority in those circuits. Those three judges easily could hold a unanimous opinion, but if the other four considered the questions they would be unanimous the other-way. If no judge dissents in the three-judges court, how is the majority to be informed, except by the necessity to study and scrutinize every record and every decision? The same is true in circuits with six judges. There, opposite opinions by two sets of three judges, would have to find a majority solution by obtaining "the attendance" of the Circuit Justice assigned to that circuit, so as to make the court *en banc* comprise seven votes. The need for every judge to concern himself with every case on the docket, equally would pertain to the circuits having five circuit judges, and even to four; adding the presence of the Circuit Justice in the latter instance would supply the necessary majority as against an otherwise "hung jury" of the four judges.

4. If the addition of judges without changing the provision in the Judicial Code relative to three judges, means that the "circuit court" comprises all of the appointed judges (as the opinion-below argues) in a judicial circuit, then "The Circuit Court of Appeals for the Third Circuit" means that *all cases* shall be considered *by five judges*. If that were true, the inquiry is proper:—How could Congress expect to clear dockets quicker by five judges courts than by three-judges courts?

5. If "three judges" in the Judicial Code, means five judges in the Third Circuit and seven judges in the Ninth Circuit (and so on), then when Congress grants an appeal or review by "the circuit court of appeals" in any taxpayer's judicial circuit, it means that *five judges* must consider every case in the Third Circuit, seven in the Ninth Circuit, and so on. We contemplate with awe, the thousands upon thousands of cases that improperly have been decided!

6. Each Justice of this Court is a "Circuit Justice" designated to a judicial circuit, and is a member of the circuit court of that circuit "when in attendance." Thus, he is one of the *three* judges who sits as a circuit court of appeals. In other words, if the argument by opinion-below were correct, the court of the Third Circuit is not *three* judges, but five circuit judges *and a Circuit Justice*. If any question is so important as to require consideration by a "full court" of five judges, why is it not important enough to require attendance by "*the full court*" of six judicial appointments? Answer; if Mr. Justice Roberts, as the Circuit Justice in the Third Circuit, had been informed that the "importance" of the questions in this case required his attendance, his *possible* agreement with Judges Maris and Goodrich would have meant a divided court,—and affirmation of the Board decision. Thus, a court *en banc* would have accomplished nothing. We do not mean by that, that the non-attendance of Mr. Justice Roberts was intentional in our case. We mean rather, that if a court *en banc* means

all persons who are qualified to be members, then in the Third Circuit (and all other circuits having odd numbers of circuit judges) no majority action can be ^{be} assured. Whereas, in the kind of court provided by the Judicial Code (three judges) a majority action *always is assured*.

7. The Judicial Code not only provides in Section 117 for a court of three judges, but also specifies "of whom two shall constitute a quorum." There is no provision that a *majority* shall constitute a quorum. So, we note, that when the Third Circuit amended its rules to validate a court *en banc*, it recognized the Judicial Code in one respect at least;—"Two judges shall constitute a quorum," even for a court *en banc*. In that regard, let us now examine Section 120 of the Judicial Code;

" . . . In case *the full court* at any time shall not be made up by the attendance of the Chief Justice or the associate justice, and the circuit judges, *one or more district judges* within the circuit shall sit in the court according to such order or provision *among the district judges* as either by general or particular assignments shall be designated by the court . . ." (Italics added)

Section 120 speaks of "the full court" as being in terms of the *three* judges previously specified in Section 117. Yet, if "the full court" means five or six judges in the Third Circuit, the district judges must be called upon to fill vacancies. Thus, by disqualification or illness of a circuit judge, the work of the district courts must be hampered by calls to sit in courts *en banc*,—noting, all this time, that "two judges shall constitute a quorum."

8. Whether a decision in a circuit court be two-to-one, three-to-two, or four-to-three, it always must be a difference *by one man's views*, and the objections to five-to-four decisions in this Court equally are pertinent. A four-to-three decision is closer in terms of percentage; than a decision two-to-one, but the lesser percentage *of one man* plays a greater part in the result. Therefore, we say,—the court

en banc idea will give no assurance for relieving this Court from necessity for considering cases. In a two-to-one decision, one man in dissent represents 33 1/3d per cent. In the four-to-three decision, the dissenters represent 42 6/7ths per cent. The one man whose views speak in terms of a majority opinion, represents 33 1/3d per cent in the first instance, 14 2/7ths per cent in the second.

There is more reason why this Court would deem *Certiorari* proper relative to one-man decisions in courts *en banc*, because *more judges* have evidenced the importance of the questions by the closeness of the vote, than if merely one-man dissents with two.

In fact, as one-man evidences greater importance as the size of a court *en banc* increases, a reference to this Court is more likely by the certification of questions, without resort to *Certiorari*.

So, we cannot perceive that a court *en banc* decision (where the vote is close) can serve any good purpose of benefit to this Court.

Where the decisions by a court *en banc* are unanimous or with one dissenter, nothing more is accomplished by a court *en banc* that could not equally be accomplished by a court of three-judges.

2. If any legal questions are deemed to be of importance sufficient to take judges from their other work for sitting as a court *en banc*, the questions should be of such importance as to require certification to this Court, by the free and voluntary action of a three-judges court. The Ninth Circuit solved the very same problem in that manner, in *Lang's Estate v. Commissioner*, 97 Fed. (2d) 867, (See, 304 U. S. 264 for the answers to the certified questions), and the judges of that circuit deemed that they had no authority, under the pertinent provisions of Statutes, to consider any case as a court *en banc*. The Ninth Circuit had greater reasons for consideration as a court *en banc*, because the decisions in that circuit would have stood in *direct conflict* by decision through a three-judges court; whereas, in the case

at bar *there were no conflicts in the Third Circuit* and, further, it is impossible to imagine any other case ever arising with relation to *the same facts* as are present in the case at bar (either in the Third Circuit or elsewhere). From the fact that this Court accepted and answered the questions in *Lang's Estate v. Commissioner*, instead of directing that the case be decided in that circuit by the court *en banc*, we find the only precedent of consideration of the matter, even indirectly.

10. The jurisdiction of the circuit court of appeals for review of Board decisions is covered by Section 1001, *et seq.*, of the Revenue Act of 1926 (Internal Revenue Code, Section 1141), which ends in part:

"Such courts are authorized to adopt rules for the filing of the petition for review, the preparation of the record for review, *and the conduct of proceeding upon such review . . .*" (Italics added)

In the Reports of both Committees of Congress, during enactment of the Revenue Act of 1926, it was stated:

"Court review—Rules of procedure.—The proceedings on review will be conducted in accordance with rules adopted by the several courts of review. The committee is convinced that *it is highly desirable that the rules be as uniform as possible*. In a desire not to impose a further burden upon the Supreme Court of the United States, the committee has decided to rely upon the possibility of *action by the conference of circuit judges* and upon recommendations submitted to the circuit courts of appeals by the board to secure this uniformity." (House Report No. 1, 69th Congress, 1st Session, page 20; Senate Report No. 52, 69th Congress, 1st Session, page 37.) (Italics added)

Obviously, there cannot be "uniformity" relative to taxpayers in various parts of our country, if courts are going to sit by three judges in one place, four in another, and so on up to seven in two of the circuits; nor, if a discretion rests with all the judges in any particular circuit as to

whether they will accord consideration by varying numbers of judges.

Further, the reports of the Conference of Judges evidence no recommendation for necessity as to any such change.

The opinion below argues that the "three judges" specified in the Judicial Code is meaningless. If *any* number of judges, down to a quorum of two judges, as the majority of judges in the various circuits may see fit to determine at times and from time to time, constitutes "the court", then *the judges* make "the court" instead of Congress, and Section 117 must be construed as being wholly meaningless. Congress "makes" the judges, but the judges make *the court*.

11. This case presents a most curious situation by way of paradox. For one purpose what Congress has declared, is disregarded; for another purpose Congress is construed as having said *something which it did not say*, but is "presumed" to have said by a silence.

12. The opinion below finds answer in the opinion of the Ninth Circuit in *Lang's Estate v. Commissioner, supra*:

"Obviously if this were a three-judge court, when five specifically and all the district judges were competent to sit to constitute a 'full' court 'Which shall consist of three judges', it is not enlarged to a four-judge or five or more judge court because there are now more circuit judges competent to participate in its sessions.

Any other interpretation of the legislation would lead to grave difficulties of administration. If, because there are four or six circuit judges in a circuit, a four or six-judge court were deemed created by Congress, then each judge may well have the right and the duty to demand his place in the hearing on each appeal. This would lead to the embarrassment of an evenly divided court. More important still, it would increase so greatly the amount of work of each individual judge that it would cause again the arrearages which the additional judges have been created to remove."

13. If all the circuit judges of a circuit can sit as "the court", it would seem to follow that all of the district judges within a circuit may sit as a "district court", or as many as the judges themselves may select. Yet, we find in Judicial Code, Section 266, as amended, provision for a three-judge court in terms of a combination as between one Circuit Justice or circuit judge, and two district or circuit judges, in specified situations. It appears that Congress holds a decided preference for three-judge courts.

14. The opinion below expresses concern regarding what may be "the circuit court of appeals" if it does not comprise all of the judges holding appointment to a particular circuit. That situation is no different from that of the *district* courts. (See, Judicial Code, Section 1, as amended.) Congress has provided for a number of "district courts" and for several judges to preside as the *same district court*. That, however, does not change the situation of a "district court" functioning by a *single district judge*. If courts *en banc* were proper for circuit courts of appeals, it equally could be argued that all of the district judges of any particular district court could sit *en banc*, regardless of the provision that they sit as single judges. Thus, not only would a lack of uniformity result but also, the very reason for additional district judges in congested district courts would find a frustration. It may be noted further, that Judicial Code, Section 118, gives a clear distinction between circuit judges and the circuit court, as follows:

" . . . it shall be the duty of each circuit judge in each circuit to sit *as one of the judges* of the circuit court of appeals in that circuit from time to time according to law. . . ." (Italics added)

What is, "according to law", except by reference to the three-judge court mentioned in Section 117? The distinction would appear clear, that circuit judges are judges for their circuit, but that they participate as judges of the circuit court of appeals when the court functions *through three judges*.

15. The Constitution (Article III, Section 1) and Acts of Congress enacted pursuant thereto, have not vested the judicial power in circuit courts of appeals (as inferior courts) comprising a greater number than three judges. When five judges in the Third Circuit purported to hear and decide this case, various groupings of the five judges can find a conversion into *ten* circuit courts of appeals as purporting to exercise the judicial power relative to the case of this petitioner. Whereas by Internal Revenue Code, Section 1142 the review of Board decisions is confined to "a circuit court of appeals", a consideration by *ten* circuit courts of appeals finds no authority by statute.

The petitioner urges the foregoing objections as rendering the judgment by the court *en banc* invalid as² being without any authority in law.

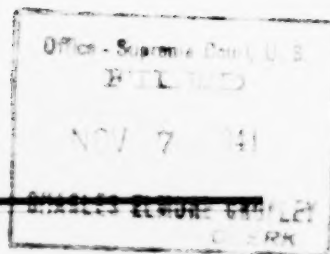
CONCLUSION.

By the entry of the appropriate judgment, the decision of the Board of Tax Appeals should be affirmed, or the judgment of reversal by the court *en banc* should be set aside and the Circuit Court of Appeals for the Third Circuit should be ordered and directed to enter judgment for the petitioner herein affirming the decision of the Board of Tax Appeals, or, if this Honorable Court deems that the ends of justice so require, the case should be remanded to the Board of Tax Appeals for a rehearing.

Respectfully submitted,

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FILE COPY



IN THE
Supreme Court of the United States

OCTOBER TERM, 1941.

No. 34.

TENTILE MILLS SECURITIES CORPORATION, *Petitioner*,

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent*.

On Writ of Certiorari to the Circuit Court of Appeals for
the Third Circuit.

REPLY BRIEF FOR THE PETITIONER.

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REPLY BRIEF FOR THE PETITIONER.

We reply to respondent's brief by two subdivisions, covering separately the deductible expenses and court *en banc*.

I.

THE EXPENSES IN PROMOTION OF THE SETTLEMENT ACT.

A.

Respondent's brief is largely a paraphrasing of the opinion by Judge Biggs in the Court below, which we covered by our main brief.

Additionally, however, it attempts the involvement of this petitioner in an atmosphere of prejudice before this Honorable Court by a note at pages 19 and 20 which contains charges and innuendos which hardly can be described as fitting or proper when counsel are supposed to assist the Court in attaining the ends of Justice.

At the time when we made our contracts with the citizens of Germany and through the enactment of the Settlement Act, Germany stood as a sister-republic which was struggling to attain its place by our side among the republics of the World. In that endeavor, the United States was helping them. The war-lords of the First World War had been eliminated into the discard, with their ideas of world domination, and "der Tag."

No Hitler, with his "Mein Kampf" and similar concepts for the destruction of humanity and world domination even stood as a faint star, visible at the horizon of world affairs through a powerful telescope.

We were dealing with peaceful people who seriously sought the establishment of a law-abiding democracy as their place in the sun, along with other law-abiding democracies.

Billions of American dollars had been and still were being poured into Germany in the aspiration for the sound establishment of their people under a democratic form of government, and with encouragement by the United States as a friendly government.

England itself was doing the same thing, working zealously for the re-creation of a New Germany, a different Germany, and a contented body of people—often against the policies or desires of France.

Right up to the start of this present war in 1939, England persisted in its policy of appeasement, not with the former peaceful people, *but with a Hitler*.

The fact that matters did not finally eventuate on the lines of the hopes of civilized and well-wishing people has no more relation to this case than do the acts of Napoleon or George the Third.

When the Settlement Act was enacted in 1928, the members of Congress and the representatives of claimants, American and German alike, had full confidence and complete expectation that the claimants on both sides would receive every last dollar of their just claims by force of performance through that Settlement Act.

Events through the passage of time proved otherwise—as to *both* sets of claimants. But the hopes, motives, and sound conclusions upon facts as existent in 1928 cannot in any sense of fairness be maligned by reason of facts *which first found existence many years after 1928*. Such a suggestion by respondent maligns equally the very same Congress of 1928 that enacted the Revenue Act which applies in this case.

If foresight ever could be equal to hindsight, this sorry World would be an Elysium. To our misfortune, it is not. If England had adopted a policy of German-domination through the decades following the Armistice, in place of its policy for German reconstruction and appeasement, the British Isles would not stand today as an armed camp, hourly threatened with annihilation by the despotism of Hitlerism, and all of Europe would not stand under control by Hitler.

If Congress could have foreseen in 1928 the things which began to occur in Germany in the 1930's, the Settlement Act never would have found enactment. Congress, not until 1935 by the Harrison Resolution, suspended further payments to Germans of claims under the Settlement Act.

Equally is it true that if this petitioner had possessed any means for anticipating the things which happened in 1927, as well as after 1928, *it never would have engaged upon the contracts of 1924*. In that event, this petitioner would not stand before this Court in this litigation.

But *we face facts*, and all of the unfair imputations in the respondent's note at pages 19 and 20 find most direct repudiation in the fact that the American claimants themselves *agreed to that Settlement Act* as the enactment into legislation of their Compromise Agreement with the Ger-

man claimants. (See petitioner's main brief, pp. 53-76.)

The respondent would make of this case an attempt to *punish* the petitioner for everything that has happened in the affairs of this unhappy world from the time that Hitler appeared on the scene and the German Republic crumbled into decay. If this Honorable Court agrees with such a concept of Justice, then the humble citizens represented in this petitioner must suffer the punishment in like degree as in the so-called "courts" of Germany and Russia. But we hold to our faith that this Honorable Court, regardless of present animosity in general against things-German, will decide this case upon its own merits, wholly divorced from the unfortunate fact that we happened to represent Germans under entirely different facts and conditions than now exist. We do not plead for Germans; we stand here as American citizens.

B.

Separated from such an attempt at prejudice, the questions presented in this case are not different, in the slightest degree, than if we stood before this Court as the representative of a poverty-stricken *American* claimant, who had no means for compensating us for services in promotion of *that very same Settlement Act* by a contingent contract whereby we advanced for him the necessary expenses, as his attorney-in-fact.

This case is no different from the situation of any lawyer who engages for the poor man to procure an appropriation by Congress by a private act of special legislation, the lawyer advancing his expenses and finding compensation only through a contingent contract.

C.

What the respondent, in effect, argues, and what the opinions of Judges Biggs and Clark by implication declare is that an Act of Congress *only must be the resort of the rich man*, who can pay cash regardless of the result, who can pay cash to the attorney in a volume sufficient to cover

all possible expenses, or who can pay the expenses directly himself upon the attorney's instructions.

They declare, however, that the *poor* man, who lacks such cash resources, must stand in the underprivileged class, deprived of all redress by Congress (or a State Legislature), because his only manner of compensating an attorney is out of the result. The *poor* man must stand without rights, without redress—*merely because he is poor*.

Their conception of Democracy is that resorts to the Sovereign for legislation, although granted and preserved in the Constitution itself, must stand solely as the right of the rich man, who has the cash and can pay the cash regardless of the accomplished result as to legislation.

The sole and only reason for contingent contracts in this case was that *the petitioner was representing the poor man*, who had no means for paying except as the result of the Act, from the funds held by the Alien Property Custodian, and restored (only to a partial extent) by the legislation.

D.

Throughout the monumental category of statutes and Acts of Congress, only one form of action has been condemned relative to contacts as between citizens and members of Congress, bribery. The giver and the receiver equally are punishable as penal offenses. (Criminal Code, Secs. 110, 111.)

"Lobbying" (whatever the term may mean), with the single exception of bribery, never has received the slightest degree of condemnation by Congress. Not even do our laws require the registration of a so-called "lobbyist" (whatever *that* term may mean).

Throughout the brief, the respondent repeatedly uses that expression "lobbying" as though it had a single, pernicious, or unfavorable interpretation with application to the petitioner.

Yet, it may be observed, in the very Article 262 of the Regulations here involved, a distinction is made between

“lobbying purposes” and “the promotion or defeat of legislation” as being disjunctive and separate forms of conduct.

Throughout petitioner’s main brief, we repeatedly have stressed and admitted that we were engaged upon “the promotion or defeat of legislation.” The Trading with the Enemy Act, by implication, invited such an activity. It was the business in which we were engaged.

We categorically and most emphatically deny that we had any connection with “lobbying” in the detrimental concept of the term, which respondent’s brief continuously tries to pin upon us, to our prejudice before this Court.

The Board itself states (R. 21, 22):

“There has been no showing that the petitioner indulged in any questionable practices in carrying out the purposes of its employment.”

The pertinent facts were found by the Board as stated in a Stipulation of Facts. (R. 29-38.) Nowhere therein can that word “lobbying” be found. It is admitted there, however, that we were engaged upon “the promotion of legislation.” (R. 30, 31, 32, 33, 34, 35, 36.)

The term “lobbying” is so exceedingly elastic as to various meanings that it serves no useful purpose by introduction into this case. The word “man” also is a term of comprehensive and varying meanings. The word may be used as inclusive of both sexes, or it may apply to the male sex alone, and in varying meanings.

Man, either as humanity in general, or a male of the species, is not to find condemnation because the Northwest Mounted Police “always get their man,” in the sense of a criminal.

Labor and farm organizations, patriotic groups, bar associations, and many other categories of interested persons may designate their representatives as “lobbyists” when seeking contacts with Congressmen as to legislation, all in commendable and helpful situations from the standpoint of

the legislation itself. But the single "black sheep" does not cast into disrepute the entire family of sheep.

By mentioning cases dealing with bribery, criminal conduct, and actions *ultra vires* as to certain businesses, the respondent attempts to characterize the petitioner as a "black sheep," instead of an innocent, peaceful member of the sheep family, as the Record shows the petitioner to have been. The ends of Justice are not achieved by subtle means for the mere "winning of cases."

E.

Respondent repeats reliance upon "the reenactment rule," but states that rule in such varying concepts that nobody can determine from the brief what they may mean—except for another attempt to "win a case."

At page 7, they state that a Treasury ruling of long standing "must be given the effect of law unless plainly in conflict with the statute." In other words, because a thing merely is *old*, it must bind this Court as law. Age was a prominent reason for the President's reorganization plan relative to this Court itself. The mere "age" by ninety-six years of precedents under *Swift v. Tyson* did not preclude the decision by this Court in *Eric Railroad v. Tompkins*. An egg may be ancient, but respect is confined to not breaking the shell.

At page 14, they state that under "the familiar rule, the successive reenactments of the statute lend even greater weight to their validity." A matter of mere "weight" is quite different from the matter of estoppel by "long-continuedness" into "the effect of law."

At page 14, again, they state that the mere age of an administrative interpretation entitles it "to great weight."

Then, at page 15, we find a Regulation of 1928 argued for interpretation, by the action of an entirely different Congress of 1936 relative to a different section of the revenue act.

One always can accord varying degrees of "weight" to interpretations by different persons, be they Courts, Boards,

attorneys of reputation for taxpayers or Government, or jurists expressing their views in legal periodicals. Even a legislative attempt in 1941 by way of interpretation of an Act of 1864 may merit a respectful consideration. But that does not answer the questions here presented. As stated by Mr. Justice Holmes in "Collected Legal Papers," p. 207:

"We do not inquire what the legislature meant; we ask only what the statute means. In this country, at least, for constitutional reasons, if for no other, if the same legislature that passed it should declare at a later date a statute to have a meaning which in the opinion of the court the words did not bear, I suppose that the declaratory act would have no effect upon intervening transactions unless in a place and case where retrospective legislation was allowed. As retrospective legislation it would not work by way of construction except in form."

The statement that an interpretation is entitled to "weight" is decidedly different from the assertion that it has "the effect of law." Anything having "the effect of law" is a law in itself.

Obviously, every administrative organization in government necessarily must interpret laws in the same, identical sense that members of the public who are affected by the laws must interpret those laws as best they can until courts of final resort have accorded conclusive, judicial interpretations. Such administrative organizations can bind the personnel of the organization to the interpretation and can inform the public. But, just as different persons at the top of the changing organizations are free to make new and different interpretations, in like manner is the public entitled freely to make its own interpretations. The courts have the final say in the matter.

Every interpretation by a reputable person may merit "weight," but calling an interpretation *conclusive* is "a horse of a different color." Respondent's brief straddles the issue.

F.

To the list of comments regarding "the reenactment rule" cited at page 36 of our main brief, we add:

Feller, Addendum to the Regulations Problem, 54 Har. L. Rev. 1311;
Griswold, Postscriptum, 54 Har. L. Rev. 1323.

The confusion in Taxation results in large measure from a Babel of tongues. Respondent's brief uses such terms as "regulation," "rulings," "lobbying," with absence at definitions.

We believe that the regulation problem would find a ready clarification if this Honorable Court would accord recognition to the clear distinction between a regulation by authority of Congress and an administrative interpretation which lacks explicit Congressional authority.

That distinction found emphasis by Mr. Alvord in his article on the subject of the regulations problem, 40 Col. L. Rev. 252. Mr. Alvord served as the Legislative Representative for the Treasury Department in 1928 relative to both the Settlement Act and the Revenue Act of 1928, following previous service with Congress as a Legislative Counsel. If "weight" means anything, it well could be applied to his article.

By recent action in the Treasury Department, since the filing of our main brief, is found confirmation of Mr. Alvord's position, which also is mentioned by Professor Griswold and Professor Feller in their articles.

The distinction is between a legislative regulation and a so-called "Regulation" that is interpretative in the sense of attempted anticipation by way of a judicial construction. Year after year the Treasury Department has published "Regulations," separately covering the varied provisions of revenue acts, including in the very same publication *legislative regulations* which specifically have been authorized by Congress in specific sections or subsections of the revenue acts, and interpretations of other sections of

the revenue acts wherein Congress *has not authorized "regulations."*

Very recently the Treasury Department has published for consideration, comments, and suggestions, what is entitled "Internal Revenue Administrative Code."

That "Code" comprises 239 pages and constitutes an attempt to separate out of the Internal Revenue Code all of the provisions that deal with matters of *administration* as to the revenue laws. That "Code" omits all phases of an *interpretative* nature.

We have made a page-by-page study of this new, proposed "Code," and have found 409 instances of provisions taken from the Internal Revenue Code, where Congress specifically has authorized "the Commissioner with the approval of the Secretary" to prescribe *legislative regulations*. The removal of those provisions, out of the Internal Revenue Code into this new Administrative Code will leave no provision for "regulations" still standing in the Internal Revenue Code, if and when Congress enacts this Administrative Code into law.

When that process for reform finds completion, any attempt thereafter at the publication of *interpretations* by the Treasury Department will stand in its clear light as nothing more than an administrative *opinion* regarding the meaning of the laws, awaiting judicial decision for the conclusive answer.

The interpretative phase of so-called "Regulations," confused as they have been in the past with "legislative regulations," always has been nothing but legal opinions. The enactment of this Administrative Code will place them in their true light, boldly stripped of the former camouflage as "Regulations."

G.

Relative to the matter of "ordinary and necessary expense," there never has been in *any revenue act* an authorization by Congress that "the Commissioner with the approval of the Secretary" may prescribe regulations relative

to the interpretation of that section of the law. Any interpretation is an ordinary function of everybody who may be affected by any law.

Whatever "Regulations" may have stated in that regard, whether under the title of "Donations," or relative to Section 23 (a), always has been nothing but an *opinion*, to be judicially corrected or approved.

The Commissioner has been given authority to determine the *reasonableness* as to salaries and compensation for services rendered. There his authority ceased, with review by the Board and courts.

Whether such *opinions* be by laymen Commissioners and Secretaries (as many of them have been), or by a succeeding Congress itself, they should speak with no more weight than non-judicial opinions in general.

"Two wrongs never make for right," and a succession of erroneous, non-judicial opinions can have no effect upon a correct judicial interpretation in the administration of Justice.

H.

Respondent's brief argues that it is not "usual" for an attorney-in-fact to advance the expenses in matters of legislation and that our undertaking comprised nothing but a "gamble."

It is "usual" for people *to perform their contract obligations*, and it was *our business* to represent those claimants under our contract commitments. There was far less of a "gamble" in the matter than are the day-by-day gambles in every other conceivable form of business undertaking. Lawyer, doctor, merchant, manufacturer, "gambles" daily as to whether his gross receipts will exceed his expenses. We, on the other hand, prior to 1924, had perceived a number of Acts of Congress which had accorded restorations to the former enemies. (See main brief, pp. 55-57.)

The element of uncertainty was whether the American claimants would prevail for a confiscation of the funds held by the Alien Property Custodian. Therein were the ex-

penses in question our necessity, by force of our contract commitments.

We advanced the expenses for the same reason, as our compensation and reimbursement for the expenses were contingent upon the result—because we performed the service *for poor men* who had no other resources than the funds to be restored by the legislation.

I.

Respondent's brief declares that we did not sustain the burden of proof that those expenses were "ordinary and necessary."

We categorically deny the statement at page 7 of "the Commissioner's determination that these were not 'ordinary and necessary' expenses."

The Commissioner determined *no such thing*.

His sole and only determination (R. 11) was that:

"Sums spent for the promotion of legislation are not deductible from gross income in accordance with Article 262 of Regulations 74 promulgated under the Revenue Act of 1928."

The sole and only contention by the Commissioner in the Board proceeding was that ordinary and necessary expenses were not deductible *when they involved the promotion of legislation*, by reason of Article 262 and "the reenactment rule."

There, again, does the respondent's counsel indulge in tactics that would not be countenanced if in representation of any private litigant.

The Board stated (R. 18):

"At the hearing his counsel stated that 'the question in one sentence is whether the Board will follow that decision or whether it won't.' "

"That decision" was the *Sunset-Scavenger* case, which applied an interpretation of "the reenactment rule" with application to the Article 262.

That was the only litigated matter in the Board proceeding. That the expenses were "ordinary and necessary" never was questioned or disputed.

Further, the Board stated (R. 18) with reference to the respondent:

"Neither does he make any claim that the expenses incurred were not in fact ordinary and necessary in performing the services required of it under its contract."

If any taxpayer must maintain a burden of proof as to an item *not claimed* by the respondent, it is a new idea in judicial procedure.

J.

At page 16, respondent contends that the expenses would not be "ordinary" unless we proved "that enterprises of this type commonly incur expenses for lobbying activity under the type of arrangement involved here."

Unless we again wage war against Germany, evolving into a German defeat, our sequestration of private property owned by Germans, their loss of all properties located elsewhere than here, and the repetition of the same questions involving our restoration of seized property following a treaty of peace, it is impossible to imagine any "type" by way of duplication of the facts relative to our business as evidenced in this case.

As stated in *Deputy v. du Pont*, 308 U. S. 488, 496:

"One of the extremely relevant circumstances is the *nature and scope of the particular business* out of which the expenses in question accrued." (Italics added.)

Our business was the performance of contracts under facts peculiar to a particular situation. Certainly anybody else who confronted the same facts would find the same kind of contracts as a "type," and would have to perform the business in the very same way as a "type." It was typical of our *contracts*, to bear the expenses, and the performance of those contracts *was our business*.

II.

THE COURT EN BANC.

Respondent argues by brief that the circuit judges are appointed to "the *Court*," as distinct from the judicial circuit. The opinion of Judge Biggs says much the same, with mention (R. 56) of an Act of 1936 which directed the President to add a fifth judge in the third circuit: "to appoint an additional judge of the United States Circuit Court of Appeals for the Third Circuit."

The eminent Judge states (R. 56) by comment thereon:

"This act clearly contemplated an addition to the court as well as to the number of circuit judges in the circuit and confirms the construction of the statute which we have adopted."

If the Judge's search had been more thorough, he would have found that the Act of 1936 which he quoted *is the only instance* of such manner of expression relative to the Third Circuit. It represents an exception, a slip of the tongue, careless language that stands contrary to *every other Act* (except for one) authorizing the appointment of additional circuit judges in all other circuits. (See U. S. C. A., Title 28, Section 213, with supplement by Cumulative Annual Pocket Part.)

That the language in that 1936 Act was an oversight, without intention, is evident by Acts *after 1936*, which provided for additional judges in other circuits:

"The President is hereby authorized to appoint by and with the consent of the Senate, two additional judges for the ninth judicial circuit." (April 14, 1937, C. 80, 50 Stat. 64.)

"The President is authorized to appoint by and with the advice and consent of the Senate, four additional circuit judges, one for each of the following judicial circuits: Second, fifth, sixth, and seventh." (May 31, 1938, C. 290, Sec. 1, 52 Stat. 584.)

"The President is authorized to appoint, by and with the advice and consent of the Senate, three additional circuit judges as follows:

- (a) One for the sixth circuit;
- (b) Two for the eighth circuit." (May 24, 1940, C. 209, Sec. 1, 54 Stat. 219.)

The Third Circuit comprised three circuit judges until an Act of June 10, 1930 (C. 438, 46 Stat. 538) provided:

"The President is authorized to appoint, by and with the advice and consent of the Senate, an additional circuit judge for the third judicial circuit."

Every preceding Act authorizing additional circuit judges was in similar language. Every like Act after 1936 has been in that same language. (There was one other exception by an Act of 1935.)

That the Act of 1936 evidenced somebody's clerical error appears too clear for discussion, bearing in mind that the reason for all those additional circuit judges was not to enlarge courts, but to permit more expeditious decisions in congested dockets by the three-judge-courts prescribed by Judicial Code, Section 117.

Respondent's counsel (the Department of Justice) might freely have examined the Annual Reports of the Attorney General to verify that reason for recommendation of appointment of additional judges. Did the Attorney General ever recommend amendment to Section 117 so as to provide for "a court of seven judges in the Ninth Judicial Circuit," or "a court of five judges in the Third Judicial Circuit," and so on? Of course not, because the only reason for the additions was to make available more judges in respective circuits for sitting as courts in rotation *by three judges*.

If it were true that the authorization and appointment of additional judges makes "the court" comprise all the judges in respective circuits, then Section 117 must stand repealed by implication, and hearings by courts of three

judges stand without authority except in the First and Fourth Circuits. Then seven judges must sit as the court *in all cases* in the Eighth and Ninth Circuits, five judges in the Third Circuit; and, if judges cannot attend sessions, vacancies must be by assignment of district judges. And, what becomes of the provision "of whom two shall constitute a quorum"? (Judicial Code, Section 117.)

Can anybody conceive of Congress declaring that "two shall constitute a quorum" if the Court in the Eighth and Ninth Circuits must comprise *seven judges*?

The correct conclusion appears to be that "a court" presides for hearing and decision in a specific "case or controversy." The composition of such Court is found from Congressional direction regarding the judges who are qualified to preside in according the litigants their "day in Court."

In the Circuit Courts of Appeals, those qualified judges are found in circuit judges, Circuit Justices, and in district judges, under designated conditions.

A court exists only relative to the respective litigants in a particular case or controversy. Apart from actual litigants, it is impossible to conceive of "a court," except as a potentiality for future resort.

Congress has prescribed circuit courts of appeals as comprising three qualified judges. Until Congress declares otherwise, there is no authority in the circuit judges to create courts of a greater number than three judges.

That the circuit judges themselves question their authority in that regard is evident from the bills which they have advocated in the House and the Senate with present pendency.

At the hearings on S. 1053 before a subcommittee of the Committee on the Judiciary United States Senate on April 23, 1941, judges were the witnesses. In the published report at page 40, Judge Groner stated:

"* * * The question has been discussed in the conference of judges three or four times * * * and there was a difference of opinion. Judge Biggs up in Del-

aware is of the opinion that it can be done, and did do it, and his judges concurred with him. They sat in two or three cases recently. I think Judge Hand expressed some doubt as to whether it could be done, and some other judges, I forget how the vote went around, or the discussion went around, *but there was a very decided opinion that it could not be done * * ** (Italics added.)

The S. 1053 was introduced in the Senate a day or so after our Petition for Certiorari was filed.

We recite these facts for such "weight" as the "very decided opinion" of the Conference of Judges may merit.

Respectfully submitted,

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No. 812 34

In the Supreme Court of the United States

OCTOBER TERM, 1940

TEXTILE MILLS SECURITIES CORPORATION, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL
REVENUE

*ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED
STATES CIRCUIT COURT OF APPEALS FOR THE THIRD
CIRCUIT*

MEMORANDUM FOR THE RESPONDENT

In the Supreme Court of the United States

OCTOBER TERM, 1949

No. 812

TEXTILE MILLS SECURITIES CORPORATION, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL
REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED
STATES CIRCUIT COURT OF APPEALS FOR THE THIRD
CIRCUIT

MEMORANDUM FOR THE RESPONDENT

We do not oppose the granting of a writ of certiorari in this case.

There are two major questions presented:

1. Whether a circuit court of appeals may be composed of all the circuit judges of the circuit in active service, more than three in number, sitting *en banc*.

2. Whether there may be deducted as an ordinary and necessary expense under Section 23 (a) of the Revenue Act of 1928 payments to persons engaged

by the taxpayer to provide publicity and prepare propaganda as an aid to the taxpayer's undertaking, pursuant to a contingent fee contract, to obtain the enactment of congressional legislation beneficial to its principal.

The first question raises an important issue as to the structure of the circuit courts of appeals. It is in the public interest that the question be authoritatively settled, particularly since the decision below in this respect is contrary to the views expressed in *Lang's Estate v. Commissioner*, 97 F. (2d) 867, 869 (C. C. A. 9th).

If the petition is granted, we do not oppose review of the second question, in order that the merits of the tax controversy may also be before the Court. In the event that the Circuit Court of Appeals be reversed on the procedural and jurisdictional point, a determination of the substantive issue would become desirable in order to facilitate disposition of the proceeding. It would avoid questions that might otherwise arise, in view of the differing opinions held by the judges of the Circuit Court of Appeals, as to the status of the case and its future consideration.

The question on the merits does not, however, present any direct conflict among the circuits, as alleged by petitioner (Pet. 12). The decision below is in accord with a similar result reached in *Sunset Scavenger Co. v. Commissioner*, 84 F. (2d) 453 (C. C. A. 9th), where deductions for lobbying

expenses were denied. Cf. *Old Mission P. Cement Co. v. Commissioner*, 69 F. (2d) 676, 681 (C. C. A. 9th),¹ affirmed on other issues, 293 U. S. 289.² Although deductions have been allowed, erroneously, we believe, in two somewhat comparable cases in the Fifth Circuit, the court nevertheless indicated that it regarded as distinguishable cases involving lobbying or contracts that are unenforceable as against public policy. *Lucas v. Wofford*, 49 F. (2d) 1027, 1028; *Alexandria Gravel Co. v. Commissioner*, 95 F. (2d) 615, 616. Two other circuit court of appeals decisions alleged (Pet. 12) to be in conflict, *Sullivan v. United States*, 15 F. (2d) 809, 810 (C. C. A. 4th), and *Steinberg v. United States*, 14 F. (2d) 564 (C. C. A. 2d), must be read in the light of this Court's reversal of the *Sullivan* decision (274 U. S. 259) and the decision of the Circuit Court of Appeals for the Second Circuit, subsequent to the *Steinberg* case, in *Burroughs Bldg. Material Co. v. Commissioner*, 47 F. (2d) 178.

There is no conflict, moreover, on the question of the validity of the contracts here in question. The cases cited at page 12 of the petition for certiorari

¹ In the light of these decisions by the Circuit Court of Appeals for the Ninth Circuit it is plain that *Heleering v. Hampton*, 79 F. (2d) 358 (C. C. A. 9th), relied upon by petitioner (Pet. 12), does not present a conflict. The *Hampton* case involved the deductibility of amounts paid on a rescission suit, and is not regarded by the same court as a precedent with respect to lobbying expenses.

² This Court in effect denied certiorari on this issue in the *Old Mission* case when it limited the writ (293 U. S. 544).

deal with undertakings that are readily distinguishable. As the court pointed out, contracts virtually identical with those now in issue were recently held unenforceable by the Court of Appeals for the District of Columbia, and certiorari was denied. *Gesellschaft Fur Drahtlose Telegraphie, M. B. H. v. Brown*, 78 F. (2d) 410, certiorari denied, 296 U. S. 618; *Brown v. Gesellschaft Fur Drahtlose Telegraphie, M. B. H.*, 104 F. (2d) 227, certiorari denied, 307 U. S. 640.

The Circuit Court of Appeals decided that as a matter of law expenses of the character in question were not ordinary and necessary within the meaning of Section 23 (a) of the statute. In thus reversing the Board of Tax Appeals, the court did not, as alleged in the petition (p. 13), depart from the accepted course of judicial procedure, or shift the ground upon which the case had previously been considered.

Respectfully submitted.

FRANCIS BIDDLE,
Solicitor General.

MARCH 1941.

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No. 34

In the Supreme Court of the United States

OCTOBER TERM, 1941

FENTLE MILLS SECURITIES CORPORATION, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL
REVENUE

*A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT
COURT OF APPEALS FOR THE THIRD CIRCUIT*

BRIEF FOR THE RESPONDENT

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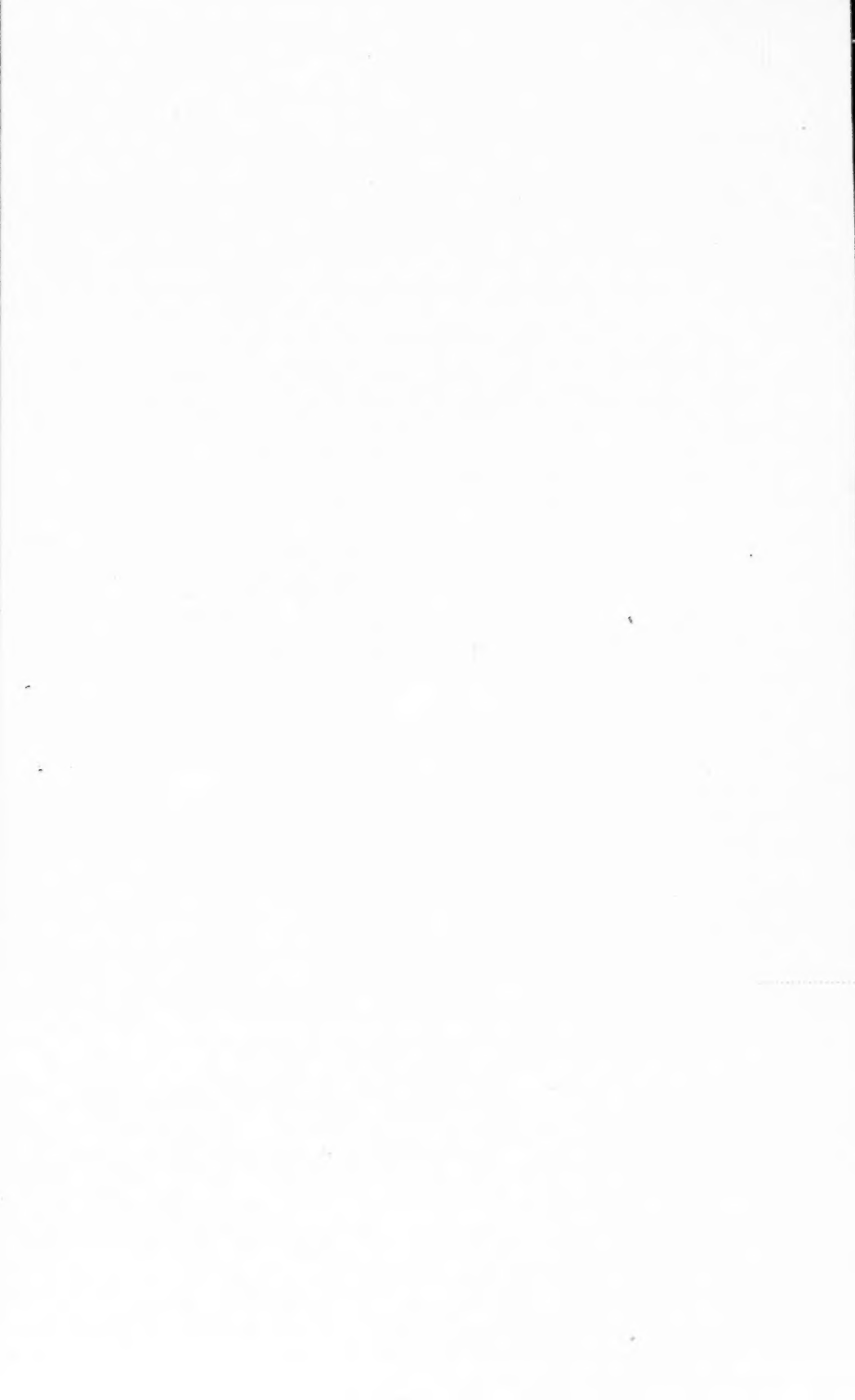
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In the Supreme Court of the United States

OCTOBER TERM, 1941

No. 34

TEXTILE MILLS SECURITIES CORPORATION, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL
REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT
COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE RESPONDENT

OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 13-23) is reported in 38 B. T. A. 623. The opinion of the Circuit Court of Appeals (R. 42) is reported in 117 F. (2d) 62.

JURISDICTION

The judgment of the Circuit Court of Appeals reversing the decision of the Board of Tax Appeals was entered December 7, 1940 (R. 75), and its judgment denying the subsequent motion of

the taxpayer for a judgment affirming the decision of the Board of Tax Appeals was entered January 3, 1941 (R. 79). The petition for certiorari was filed March 5, 1941, and was granted March 31, 1941 (R. 80). The jurisdiction of this Court is conferred by Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. Whether there may be deducted as an ordinary and necessary expense under Section 23 (a) of the Revenue Act of 1928 payments to persons engaged by the taxpayer to provide publicity and prepare propaganda as an aid to the taxpayer's undertaking, pursuant to a contingent fee contract, to obtain the enactment of congressional legislation beneficial to its principal.

2. Whether a circuit court of appeals may be composed of all the circuit judges of the circuit in active service, more than three in number, sitting *en banc*.

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved are set forth in the Appendix, *infra*, pp. 53-60.

STATEMENT

This case involves income tax liability of the petitioner and was brought to the court below by the Government's petition to review an order of the Board of Tax Appeals. The case was origi-

nally heard below by a court composed of three circuit judges. Thereafter, that court acting pursuant to its Rules 4 and 5, *infra*, pp. 59-60, entered an order restoring the case to the calendar for reargument before the court *en banc* (R. 41). The case was then heard by a court composed of the five circuit judges in the circuit in active service. The decision of the court was in favor of the Government with two judges dissenting. The taxpayer thereupon filed a motion for the entry of a judgment in its favor to be ordered by a court comprised of the two dissenting judges; but those two judges themselves denied the motion (R. 76-79).

The facts relating to petitioner's income tax liability, as stipulated (R. 29-38), and found by the Board (R. 14-17), may be summarized as follows:

The taxpayer, a Delaware corporation, was engaged in various business activities, including trading in securities, investing in domestic and foreign properties, and acting as agent for foreign and domestic principals (R. 14, 29). Its officers, who were also its sole stockholders, were officers, directors, or stockholders of one or more manufacturing corporations in the textile industry (R. 29-30).

In 1924 the taxpayer, through personal contacts of its officers, was employed to represent certain German textile interests whose properties in the

United States had been seized during the World War under the provisions of the Trading with the Enemy Act, October 6, 1917, 40 Stat. 411. The purpose of the employment was to procure legislation which would permit the ultimate recovery of the properties. The properties had an aggregate value of \$60,000,000. It was agreed that the taxpayer would bear all costs and expenses incident to the undertaking, and would receive as compensation ten per cent of the amount or value of such property as it might succeed in recovering. The contracts would terminate at the close of the second session of the Sixty-ninth Congress unless in the meantime appropriate legislation had been enacted (R. 14).

In conducting the campaign to procure the enactment of the desired legislation, the taxpayer engaged the services of various persons and organizations, including Ivy Lee, Warren F. Martin, and J. Reuben Clark.¹ The Ivy Lee organization was employed to handle matters of publicity, including the making of arrangements for speeches, and contacting the press in respect of editorial comments and news items. Warren F. Martin, a former special assistant to the Attorney General and J. Reuben Clark, a former solicitor of the State Department, were employed in connection with the preparation of propaganda con-

¹ References are also made in the stipulation and the Board's findings to the activities of F. W. Mondell, but there is no issue before the Court as to deduction for payments to him.

cerning international relations, treaty rights, and the historical policy of the United States relative to enemy-owned property in time of war (R. 14-15).

A bill for the settlement of war claims was introduced and passed the House of Representatives during the second session of the Sixty-ninth Congress and was favorably reported to the Senate by the Senate Finance Committee, but had not passed that body when Congress adjourned on March 4, 1927 (R. 15).

Thereafter, and prior to the opening of the first session of the Seventieth Congress on December 5, 1927, the taxpayer undertook to negotiate new contracts similar in terms to those which had expired. New contracts were procured from many of its former principals, but on less favorable terms. The new contracts provided for the payment of 3 per cent of the amount or value of property received by the claimant and for an additional 2 per cent in respect of money or property paid over to the claimant within one year after enactment of the desired legislation. They also required that the taxpayer pay all costs and expenses. The new agreements were to run for a period of three years beginning January 1, 1928² (R. 15).

Without further arrangement or agreement, Lee, Martin, and Clark continued their work after

² An example of the new contract appears at R. 32-34.

the close of the second session of the Sixty-ninth Congress on March 4, 1927. The objective of the campaign was accomplished during the Seventieth Congress by the passage of the Settlement of War Claims Act of 1928, March 10, 1928, 45 Stat. 254 (R. 15-16).

During 1929 Ivy Lee was credited on the taxpayer's books with \$50,000 for services rendered in connection with the contracts mentioned, and payments in respect to that sum were made to him. In its return, however, the taxpayer claimed as a deduction only \$45,000 of the \$50,000 item. In 1930 Martin and Clark were credited on the taxpayer's books with \$40,000 and \$7,500, respectively, as compensation for services rendered in connection with the above contracts and the amounts so credited were taken by the taxpayer as deductions on its 1930 return (R. 16). The taxpayer kept its books and filed its income tax returns on the accrual basis of accounting (R. 29).

The deductions thus taken in 1929 and 1930 exceeded the taxpayer's net income, thereby producing a net loss in each of those years. (R. 9-10.) Pursuant to statutory provisions then in force (Section 117 of the Revenue Act of 1928, 45 Stat. 791), a net loss could be carried forward two years and applied against income for such succeeding years. The tax year here involved is the year 1931, and the question presented is whether the deductions were properly taken in 1929 and

1930, since the net losses resulting therefrom would wipe out petitioner's 1931 taxable income (R. 16).

In determining the deficiency here involved the Commissioner reduced the net losses for 1929 and 1930 by disallowing the deductions claimed in respect to the amounts credited to Lee, Martin, and Clark. The Board of Tax Appeals expunged the deficiency (R. 17), but its judgment was reversed by the court below (R. 75).

SUMMARY OF ARGUMENT

I

The decision of the court below denying the deductions for lobbying expenses was clearly correct. The taxpayer has the burden of overcoming the Commissioner's determination that these were not "ordinary and necessary" expenses. *Welch v. Helvering*, 290 U. S. 111. It has not carried that burden here. Moreover, the Commissioner's determination is supported by official Treasury rulings of long standing which must be given the effect of law unless plainly in conflict with the statute.

Even apart from the regulations, there is no basis for reversal of the Commissioner's determination that these expenses were not "ordinary and necessary." The expenditures were incurred in an undertaking of a character which cannot be said to have been of common and frequent occurrence in the type of business in which the tax

payer was engaged. Corporate funds are not ordinarily advanced on a broad gamble, pursuant to a contract of at least doubtful legality, that the enactment of legislation favorable to the claims of foreign principals can be obtained. Moreover, this point aside, it cannot be said that it is an "ordinary and necessary" expense of an appeal to Congress that funds be spent for the employment of so-called public relations counsel, etc. for the preparation and dissemination of propaganda.

Decisions in numerous analogous cases support the view that expenditures of an illegal character or with respect to an enterprise against public policy are not "ordinary and necessary" within the meaning of the statute.

II

Under Section 117 of the Judicial Code, it is provided that a circuit court of appeals "shall consist of three judges, of whom two shall constitute a quorum." By a 1912 amendment to Section 118 it is provided that "The circuit judges in each circuit shall be judges of the circuit court of appeals in that circuit * * *." The court below construed the 1912 amendment of Section 118 as impliedly modifying Section 117 so that each court should consist of the total number of circuit judges within the circuit.

We think that it is dubious whether the 1912 amendment was intended to accomplish that

result, and inferences to be drawn from the face of the statute are, at best, conflicting. However, there are strong considerations of public policy in support of the result reached by the court below, and since the interpretation is a permissible one, we urge that it be approved by this Court.

ARGUMENT

I

THE DEDUCTIONS ON ACCOUNT OF LOBBYING EXPENSES WERE PROPERLY DISALLOWED

1. Petitioner incurred various expenses for lobbying which it seeks to deduct from gross income as "ordinary and necessary" expenses under Section 23 (a) of the Revenue Act of 1928. At the very outset it should be borne in mind that, since deductions from gross income are a matter of legislative grace, the taxpayer has the burden of establishing the right to the deduction. *New Colonial Co. v. Helvering*, 292 U. S. 435, 440; *White v. United States*, 305 U. S. 281, 292. And it is firmly settled that deductions or exemptions must be construed strictly against one claiming the benefit thereof. "There must be no doubt or ambiguity in the language used upon which the claim to the exemption is founded. It has been said that a well-founded doubt is fatal to the claim; * * *." *Bank of Commerce v. Tennessee*, 161 U. S. 134, 146; see also *United States v. Stewart*, 311 U. S. 60, 71.

The question in the instant case can perhaps be most profitably explored against the background of this Court's decision in *Welch v. Helvering*, 290 U. S. 111, which contains probably the most comprehensive and authoritative judicial consideration of what constitutes an "ordinary and necessary" expense. There the taxpayer had been an officer in a corporation which had been adjudged an involuntary bankrupt and relieved of its debts. Thereafter, the taxpayer began to transact business on his own account and, in order to reestablish relations with customers whom he had known when acting for the corporation, undertook voluntarily to pay the corporate debts. The Commissioner of Internal Revenue ruled that such payments were not deductible from taxable income as ordinary and necessary expenses. This Court assumed that the expenses were "necessary," but sustained the Commissioner since they were not "ordinary." Mr. Justice Cardozo said (pp. 114-115):

Men do at times pay the debts of others without legal obligation or the lighter obligation imposed by the usages of trade or by neighborly amenities, but they do not do so ordinarily. * * *. Here, indeed, as so often in other branches of the law, the decisive distinctions are those of degree and not of kind. One struggles in vain for any verbal formula that will supply a ready touchstone. The standard set up by the

statute is not a rule of law; it is rather a way of life. Life in all its fullness must supply the answer to the riddle.

The Commissioner of Internal Revenue resorted to that standard in assessing the petitioner's income, and found that the payments in controversy came closer to capital outlays than to ordinary and necessary expenses in the operation of a business. His ruling has the support of a presumption of correctness, and the petitioner has the burden of proving it to be wrong. *Wickwire v. Reinecke*, 275 U. S. 101; *Jones v. Commissioner*, 38 F. (2d) 550, 552. Unless we can say from facts within our knowledge that these are ordinary and necessary expenses according to the ways of conduct and the forms of speech prevailing in the business world, the tax must be confirmed. But nothing told us by this record or within the sphere of our judicial notice permits us to give that extension to what is ordinary and necessary. * * *

2. The lobbying expenses in the instant case similarly fail to qualify as "ordinary and necessary" expenses within the statute. Here, as in the *Welch* case, the Commissioner has ruled that the expenditures are not deductible, and his determination must stand unless, in the language of that decision, the Court can say from facts within its knowledge "that these are ordinary and necessary expenses according to the ways of conduct and the forms of speech prevailing in

the business world." That petitioner cannot meet the burden recognized in the *Welch* case and that judicial notice can hardly produce the facts necessary to overcome the Commissioner's determination seem almost too clear for serious dispute. Moreover, as will be shown, *infra*, p. 17, contracts for procuring the very legislation involved in these lobbying expenditures have been held to be against public policy and therefore illegal. This additional fact alone when considered in the light of the familiar practices of lobbyists would justify the Court in refusing to treat these expenses as "ordinary," wholly apart from any prior determination of the Commissioner.

But in this case we have more than a mere determination of the Commissioner that these expenses are not deductible: There is present here an official Treasury regulation of long standing which in unambiguous language declares that expenditures "for lobbying purposes, the promotion or defeat of legislation, * * * are not deductible from gross income." Article 262 of Regulations 74

From almost the inception of the present income-tax law, the Treasury has ruled that amounts spent for lobbying are not "ordinary and necessary expenses." The first published ruling appeared in a Treasury Decision, dated January 30, 1915, which declared that "Sums of money expended for lobbying purposes and contributions

for campaign expenses are held not to be an ordinary and necessary expense in the operation and maintenance of the business of a corporation, and are therefore not deductible from gross income * * *." T. D. 2137, 17 Treasury Decisions, Internal Revenue, pp. 48, 57-58. This determination, elaborated to refer expressly to expenditures for "the promotion or defeat of legislation," and "the exploitation of propaganda" was incorporated as Article 143 in Regulations 33 (Revised, 1918). The regulation assumed its present form in Article 562 of Regulations 45, under the Revenue Act of 1918, and has since appeared, without change, in all successive regulations.³ See Article 562 of Regula-

³ Petitioner makes much of the fact that Article 262 of Regulations 74 under the 1928 Act, here involved, is entitled "Donations" and deals in large part with charitable contributions by corporations (Br. 26 *et seq.*). But the specific provisions of the regulations relied upon by the Government had their origin in T. D. 2137 and Article 143 of Regulations 33, where it was expressly stated that they were an interpretation of the phrase "ordinary and necessary."

Beginning with the Revenue Act of 1921, the provisions were incorporated for reasons of convenience in the Article entitled "Donations." Prior to 1928, there were separate provisions in the revenue acts dealing with expenses allowable to individuals and expenses allowable to corporations, though the provisions were identical. See, e. g. Sections 214 (a) (1) and 234 (a) (1) of the Revenue Act of 1926. Moreover, the revenue acts provided for deductions to individuals on account of charitable contributions, but made no such provision for similar donations by corporations. However, it was recognized that such donations might, in some circum-

tions 62, 65 and 69; Article 262 of Regulations 74 and 77; Article 23 (o)-2 of Regulations 86; and Article 23 (q)-1 of Regulations 94 and 101, promulgated under the Revenue Acts of 1921, 1924, 1926, 1928, 1932, 1934, 1936, and 1938, respectively.

The regulations thus represent a contemporaneous and long-continued administrative interpretation of the statute. Not only are they entitled to great weight as such but, under the familiar rule, the successive reenactments of the statute lend even greater weight to their validity. Cf. *Morgan v. Commissioner*, 309 U. S. 78, 81; *Helvering v. Winnill*, 305 U. S. 79, 83; *Old Mission Co. v. Hel-*

stances, qualify as "ordinary and necessary" business expenses of a corporation. Accordingly, there appeared in the regulations, under the statutory provisions relating to corporate deductions, an article indicating when such donations were deductible as expenses; and since lobbying expenses were thought to be loosely related to such contributions the provisions dealing therewith were likewise incorporated in the same article. But it is clear that the article was spelling out when such expenditures might or might not be deductible as "ordinary and necessary" business expenses.

In 1928, the structure of the revenue act was simplified, and expense deductions for corporations as well as individuals were incorporated in a single section, namely, Section 23 (a). Under the reorganized structure, charitable contributions by individuals were dealt with in Section 23 (n), and for functional reasons only, it was thought to be more desirable to continue the regulations here involved in juxtaposition with regulations construing Section 23 (n). But it is clear from the origin of these provisions as well as their content that they are concerned with the question whether lobbying expenses are deductible as "ordinary and necessary" business expenses.

vering, 293 U. S. 289, 293, 294. The Circuit Court of Appeals for the Ninth Circuit has so held with respect to the very regulations here involved. *Sunset Scavenger Co. v. Commissioner*, 84 F. (2d) 453; cf. *Old Mission P. Cement Co. v. Commissioner*, 69 F. (2d) 676, 681.⁴

That the regulations are in accord with the understanding of Congress is further confirmed by the enactment of Section 23 (q) of the Revenue Acts of 1936 and 1938. Prior to 1936, a charitable contribution by a corporation was deductible only if it could be treated as an "ordinary and necessary" business expense. Cf. *Helvering v. Evening Star Newspaper Co.*, 78 F. (2d) 604 (C. C. A. 4th), certiorari denied, 296 U. S. 628; Article 23 (o)-2 of Regulations 86, promulgated under the Revenue Act of 1934. Section 23 (q) now specifically permits such deductions, within specified limits, provided that "no substantial part of the activities" of the donee "is carrying on propaganda, or otherwise attempting, to influence legislation." Implicit in this proviso is the assumption that funds otherwise used for such purposes are not deductible. In the very least, it reflects a Congressional policy, which is relevant in construing the cognate provisions in Section 23 (a). Cf. *United States v. Pleasants*, 305 U. S. 357, 362, 363;

⁴ Affirmed on other issues, 293 U. S. 289. This Court, in effect, denied certiorari on this issue in the *Old Mission* case when it limited the writ. 293 U. S. 544.

Keifer & Keifer v. R. F. C., 306 U. S. 381, 391.

3. Apart from the regulations and the determination of the Commissioner, it cannot be concluded that the undertaking, which gave rise to these expenses, was "of common or frequent occurrence" in the type of business in which the taxpayer was engaged. *Deputy v. du Pont*, 308 U. S. 488, 495. The taxpayer, according to the stipulation of facts, was engaged "in various business activities, including trading in securities, investing in domestic and foreign properties, and acting as agent for foreign and domestic principals" (R. 29). There is nothing to indicate that enterprises of this type commonly incur expenses for lobbying activity under the type of arrangement involved here.

The taxpayer undertook to represent the various foreign principals on the basis of a broad gamble. It would endeavor to procure the enactment of legislation, favorable to its principals, solely on a contingent basis, and it would advance all costs and expenses. Unless the taxpayer were successful, it would receive nothing for its efforts, and it would be out of pocket whatever the costs might be. On the other hand, if it were successful, it would share on a percentage basis in a recovery which could reach almost astronomical proportions.

Speculation, of course, is not unusual in business, and paid lobbyists are a familiar phenom-

enon. But it has long been recognized that the two do not mix. And it has twice been held that contracts similar to the taxpayer's for services in connection with the very same legislation were illegal. *Gesellschaft Fur Drahtlose Telegraphie, M. B. H. v. Brown*, 78 F. (2d) 410 (App. D. C.), certiorari denied, 296 U. S. 618; *Brown v. Gesellschaft Fur Drahtlose Tel., M. B. H.*, 104 F. (2d) 227 (App. D. C.), certiorari denied, 307 U. S. 640. That result is in accord with the numerous decisions holding invalid contingent-fee contracts to procure the enactment of legislation or government contracts. E. g., *Crocker v. United States*, 240 U. S. 74; *Hazelton v. Sheckells*, 202 U. S. 71; *Trist v. Child*, 21 Wall. 441; *Marshall v. Baltimore & Ohio Railroad Co.*, 16 How. 314; *Noonan v. Gilbert*, 68 F. (2d) 774 (App. D. C.). Even if, as some contend, the mere fact of contingency is not sufficient to make the undertaking illegal, it is nevertheless a strong circumstance,⁵ and in this case it is coupled with the further fact that the taxpayer was itself to finance the undertaking, an added factor which would certainly make for illegality.

But whether or not this type of undertaking has otherwise been condemned as against public policy, and whether or not the agreement would be enforceable as between the taxpayer and its prin-

⁵ See 6 Williston on Contracts (Rev. Ed. 1938) 4881-4882; Restatement of Contracts, Sec. 563.

cipals, it is evident that the engagement was of an uncommon character. In normal business operations, even those which include representation of foreign concerns, corporate assets are not ordinarily expended on the gamble that particular Congressional action can be obtained for the benefit of such concerns. Only an excess of cynicism can warrant the conclusion that such operations normally embrace undertakings of at least questionable validity and of at least dubious social and political implications. Irrespective of the explanation that may be advanced for the terms on which the taxpayer entered into the arrangement, it can only be regarded as an unusual one.

Moreover, even if it is assumed that this was an undertaking of a common and frequent type, certainly these particular expenditures are not the "ordinary" expenses of an appeal to Congress. The deductions here involved relate solely to fees for publicity and propaganda. Publicists and propagandists at times perhaps do play an important role in connection with efforts to obtain legislative action. It may well be that it was "helpful" to the taxpayer, in its efforts here, to expend funds for the services of a so-called public-relations counsel to handle matters of publicity "including the making of arrangements for speeches and speakers around the country, cooperating with the Press in editorial comments, as well as news items, and work of a general public-

ity nature" (R. 31). It may also well be that it was helpful to expend funds for the preparation "of propaganda concerning international relations, treaty rights, and the historical policy of the United States relative to enemy-owned property in times of war" (R. 31). Elaboration of the vicious tendencies inherent in this type of high-pressure tactics is not necessary here.* They

* That the type of legislation procured by such tactics frequently turns out against the public interest is strikingly illustrated here. The petitioner represented German aliens — whose property had been seized by the United States during the World War. Although it was probably contemplated that such property would ultimately be restored to the original owners, it was meanwhile being held as security against the large claims that this country had against Germany arising out of the war, such as claims with respect to German sabotage of American industry, German seizure of American property, etc. The Joint Resolution of July 2, 1921 (42 Stat. 105), which terminated the war between the two countries, reserved to the United States and its nationals all rights, indemnifications and damages to which they were entitled under the Treaty of Versailles; and the peace treaty which followed, the Treaty of Berlin, concluded on August 25, 1921 (42 Stat. 1939), secured to the United States the rights reserved under the Joint Resolution, and recognized that the seized German property would be held until the German Government should make suitable provision for the satisfaction of the American claims. Thereafter, on August 10, 1922, in pursuance of the Treaty of Berlin, the United States and Germany entered into an Agreement (42 Stat. 2200) providing for the establishment of a Mixed Claims Commission to ascertain the amount to be paid by Germany in satisfaction of its financial obligations to the United States. Although the Commission had not yet completed its work and although there were still outstanding large American claims that had

were sufficiently summarized by the court below when it said (R. 46-47):

Obviously these news items and editorial comments did not appear under the stated sponsorship of the taxpayer or its clients. The reader of such news comments and editorials including members of Congress could not have known that they emanated from a source inspired by self-interest. Such practices tend to poison public opinion and should be condemned.

The decisive fact is that petitioners seeking relief from Congress daily present their cases without this form of insidious assistance. There is therefore no foundation for the contention that ex-

not yet been satisfied, there developed a strong movement inspired from German sources to persuade Congress to return the German property at once. That movement culminated in the Settlement of War Claims Act of 1928, 45 Stat. 254, which was the object of petitioner's lobbying contracts. Under that statute 80% of the German property was returned and only 20% together with certain other funds was retained to pay the awards of the Mixed Claims Commission. In lieu of the property returned Germany gave its unsecured obligations. However, it soon became apparent that the claims of the American nationals were far in excess of the funds available for payment of the American claims, and that Germany would not live up to her promise contained in the unsecured obligations. Accordingly, many millions of dollars in American claims remain unpaid to this day and that legislation has produced such ironic litigation as *Z. & F. Assets Corp. v. Hull*, 311 U. S. 470 (the *Black Tom* and *Kingsland* cases), in which American award-holders have competed with each other for the remaining insufficient funds.

penditures for such purposes are the "ordinary" incidents of a legislative appeal.

4. Finally, the correctness of the result below is confirmed by a number of decisions denying the deduction of expenditures incurred in connection with an activity which was illegal or contrary to public policy. Those decisions, while not necessarily conclusive, are helpful in showing that such expenditures cannot be regarded as "ordinary" within the meaning of the statute.

Thus it has been held that fines or penalties paid by the taxpayer as a consequence of statutory violations or legal expenses incurred in an unsuccessful defense of a criminal prosecution, are not deductible even though proximately connected with the taxpayer's business. *Barroughs Bldg. Material Co. v. Commissioner*, 47 F. (2d) 178 (C. C. A. 2d) (violation of state price-fixing laws); *Great Northern Ry. Co. v. Commissioner*, 40 F. (2d) 372 (C. C. A. 8th), certiorari denied, 282 U. S. 855 (violation of federal statute and regulations in operation of railroad); *Chicago, R. I. & P. Ry. Co. v. Commissioner*, 47 F. (2d) 990 (C. C. A. 7th), certiorari denied, 284 U. S. 618 (violation of Safety Appliance Act); *Tunnel R. R. v. Commissioner*, 61 F. (2d) 166, 173-174 (C. C. A. 8th), certiorari denied, 288 U. S. 604 (violations of Safety Appliance Act and the Twenty-Eight Hour Live Stock Act); *Gould Paper Co. v. Commissioner*, 72 F. (2d) 698, 702 (C. C. A. 2d) (fees in

antitrust proceedings). Cf. *National Outdoor Advertising Bureau v. Helvering*, 89 F. (2d) 878 (C. C. A. 2d); *United States v. Jaffray*, 97 F. (2d) 488 (C. C. A. 8th), affirmed on other issues *sub nom. United States v. Bertelsen & Petersen Engineering Co.*, 306 U. S. 276. See also *Bonnie Bros., Inc. v. Commissioner*, 15 B. T. A. 1231; *Levenstein v. Commissioner*, 19 B. T. A. 99; *Columbus Bread Co. v. Commissioner*, 4 B. T. A. 1126; *Achelis v. Commissioner*, 28 B. T. A. 244; *Sanitary Earthenware Specialty Co. v. Commissioner*, 19 B. T. A. 641; *Atlantic Terra Cotta Co. v. Commissioner*, 13 B. T. A. 1289; *Wolf Manufacturing Co. v. Commissioner*, 10 B. T. A. 1161; *Estate of Thompson v. Commissioner*, 21 B. T. A. 568, appeal dismissed, 62 F. (2d) 1082 (C. C. A. 8th); *Lindheim v. Commissioner*, 2 B. T. A. 229.⁷ Similarly, considerations of public policy have no doubt been dominant in denying deductions on account of bribes paid by bootleggers, or expenses incurred in an illegal gambling enterprise, or payments made in response to commercial extortion (such as payments to racketeers). See *Maddas v. Commissioner*, 40 B. T. A. 572, affirmed, 114 F.

⁷ The English courts have reached similar results in applying the cognate provisions of the British Income Tax Acts. See *Inland Revenue Commissioners v. Von Glehn*, [1920] 2 K. B. 553; *Inland Revenue Commissioners v. Warnes & Co.*, [1919] 2 K. B. 444; *Ward & Co. v. Commissioners*, [1923] A. C. 145.

(2d) 548 (C. C. A. 3d); *Silberman v. Commissioner*, 44 B. T. A. 600; *Kelley-Dempsey & Co. v. Commissioner*, 31 B. T. A. 351. Cf. *United States v. Sullivan*, 274 U. S. 259, 264. And deductions for "commissions" paid to persons for their use of personal influence in obtaining public contracts have likewise been denied. *Easton Tractor & Equipment Co. v. Commissioner*, 35 B. T. A. 189; *New Orleans Tractor Co. v. Commissioner*, 35 B. T. A. 218; *Nicholson v. Commissioner*, 38 B. T. A. 190.*

The foregoing decisions are founded in large part upon public policy; they rest upon the assumption, whether implicit or explicit, that since Congress could not have intended to allow such deductions it did not intend the phrase "ordinary and necessary expenses" to embrace such expenditures. The Treasury Department has officially adopted that interpretation for over twenty-five years with respect to lobbying expenses, and the regulations embodying that interpretation have been judicially sustained. See p. 15, *supra*. They apply with particular force here since the lobbying contracts themselves were of doubtful legality and since the expenses related to the preparation and dissemination of propaganda, part of which at least was undoubtedly intended to appear as though emanating from unbiased sources.

* A somewhat contrary result was reached, erroneously, we believe, in *Alexandria Gravel Co. v. Commissioner*, 95 F. (2d) 615 (C. C. A. 5th). See comment of Judge Clark (R. 61).

WHETHER THE COURT BELOW WAS PROPERLY
CONSTITUTED

Introductory.—Section 117 of the Judicial Code (U. S. C., Title 28, Sec. 212) provides that “There shall be in each circuit a circuit court of appeals, which shall consist of three judges, of whom two shall constitute a quorum * * *.” By an amendment to Section 118 of the Code, adopted in 1912, however, it is provided that “The circuit judges in each circuit shall be the judges of the circuit court of appeals in that circuit, and it shall be the duty of each circuit judge in each circuit to sit as one of the judges of the circuit court of appeals in that circuit from time to time according to law * * *.” Act of January 13, 1912, 37 Stat. 52 (U. S. C., Title 28, Sec. 213). At the time that amendment was adopted the statute provided for four circuit judges in the Second, Seventh, and Eighth Circuits (37 Stat. 52), and at present there are more than three circuit judges in each circuit except the First and Fourth.* Although Section 117 was not amended, the court below held that

* The statutes now provide for seven circuit judges in the Eighth and Ninth Circuits, six in the Second and Sixth Circuits; five in the Third, Fifth, and Seventh Circuits; and four in the Tenth Circuit. (See the various acts whose substance is incorporated in U. S. C., Title 28, Secs. 213, 213a-213h, inclusive.)

the 1912 amendment to Section 118 must be taken to have modified Section 117 by implication; and since there are now five circuit judges in the Third Circuit, the court held that it had authority, under these provisions, to sit as a five-judge court.

We have attempted to explore fully the question raised by the decision below and are in some doubt as to the correct answer. The legislative history of the statutory provisions relied upon by the court does not, we think, support its conclusion; on the other hand, there is nothing in the legislative history which is directly contrary to the decision. The statutory provisions on their face are susceptible of the construction given them by the court, but they are equally susceptible of the other interpretation, and the conflicting inferences that may be drawn from them furnish very little aid in the solution of the problem. However, there are strong considerations of public policy supporting the result reached and, since the interpretation is a permissible one, this Court would be justified in approving the action of the court below.

In order to assist the Court in its consideration of this question, we shall set forth fully the results of our investigation. We shall discuss (1) the general background of the problem, (2) the legislative history of the provisions involved, (3) the inferences to be drawn from the face of the statute, and (4) the extrinsic considerations of public policy.

A. BACKGROUND OF THE PROBLEM

The circuit courts of appeals have ordinarily sat as courts of three judges, irrespective of the number of circuit judges in the circuit. Although it has been stated that at times in the past more than three have sat,¹⁰ only recently does it appear that attention has been focussed on the question whether the courts could properly be composed of more than that number. At least since the adoption of the Judicial Code in 1911, questions relating to the composition of those courts have generally dealt with the increase in the number of circuit judges to enable the courts more effectively to handle the volume of work before them.

In 1924, the question was expressly raised by members of the House Judiciary Committee in the course of testimony by Chief Justice Taft and Assistant Attorney General Holland in support of a bill to increase the number of circuit judges in the Eighth Circuit from four to six. H. Rep. No. 102, 68th Cong., 1st Sess., accompanying H. R. 661. But the responses were not unequivocal,¹¹ and what

¹⁰ Editorial, *Federal Circuit Courts of Appeals—Their Impracticable Organization*, 69 Central L. J. 217 (1909).

¹¹ Chief Justice Taft's testimony was as follows (p. 4):

"The CHAIRMAN. Is there not a requirement in the law * * * as to the number of judges constituting the circuit court of appeals?

"Chief Justice TAFT. Yes; there must be two judges, but they sit three in a court.

"The CHAIRMAN. Three constitute the court.

"Chief Justice TAFT. Yes; there may not be more than four to constitute the court of appeals, but two can. It is very

the final conclusion drawn by the committee may have been does not appear.

The question appears to have been raised also at the meeting of the Judicial Conference of Senior

bad practice, however, to sit with only two; it detracts from the weight of the court's opinions.

* * * * *

"The **CHAIRMAN**. It was stated here the other day * * * that the law required or limited the number to sit at three, and that being the case in the District of Columbia here, where they wanted to add some others, that it would require the law to expressly enlarge the number that might sit.

"Chief Justice **TAFT**. I looked into that, Mr. Chairman, when the question came up with reference to the use of the judges of the Court of Customs Appeals * * * and an examination of the law made me feel that special congressional authority would be required to increase the number of that court."

Then when Representative Montague raised the point with Assistant Attorney General Holland, he testified as follows (p. 6):

"Mr. **MONTAGUE**. The circuit court of appeals consists of three members?

"Mr. **HOLLAND**. Yes.

"Mr. **MONTAGUE**. More than three cannot sit in a court.

"Mr. **HOLLAND**. I so understand."

Two years previously, Chief Justice Taft, when asked for his opinion as to the desirability of increasing the number of circuit judges in the Fourth Circuit from two to three, had testified as follows (Hearings before the House Committee on the Judiciary on H. R. 10479, 67th Cong., 2d Sess., Serial 33, Part 1, p. 9):

"Mr. **MONTAGUE**. You would have the circuit courts of appeals composed entirely of circuit judges? -

"Mr. Chief Justice **TAFT**. I think that one of the defects that have arisen in the administration of the circuit courts of appeals has been the change of the personnel of the courts. It has varied the uniformity of the decisions. There is a

Circuit Judges in October 1936. The report states that, upon the proposal of Circuit Judge Wilbur, a committee was appointed "to consider the advisability of amending Section 212 of Title 28 of the United States Code [Section 117 of the Judicial Code] in relation to the constitution of the circuit courts of appeals, with particular reference to those circuits in which there are now more than three judges * * *." Report of the Judicial Conference, October Session, 1936, p. 5. In 1938, the Conference recommended an amendment to the Code so that when there were more than three judges in a circuit "the majority of the circuit judges may be able to provide for a court of more than three judges when in their opinion unusual circumstances would make such action advisable." Annual Report of the Attorney General, 1938, p. 23. The recommendation was renewed by the Conference in 1939 and again in 1940. Annual

good deal of human nature in judges, and it helps to have the same court sitting together. If you have four circuit judges who sit together, that defect is reduced a good deal, because they are always together; but where you call in district judges that condition is disturbed, and it is not as wise a method of providing for the court as when you have a solid court constantly sitting. As I say, I was very glad to see that in the Senate bill they added to what you have done in the additional judge bill by putting another circuit judge in the fourth circuit."

But whether, in view of the fact that the circuit courts of appeals were customarily composed of three judges, he had in mind that all four judges should sit on individual cases at the same time seems doubtful.

Report of the Attorney General, 1939, p. 15; *Id.*, 1940, p. 24.

Thereafter, in response to the recommendations of the Conference, a bill was introduced during the present session of Congress in both the House (H. R. 3390) and the Senate (S. 1053) to amend Section 117 of the Judicial Code so as to read:

SEC. 117. There shall be in each circuit a circuit court of appeals, which shall consist of three judges, of whom two shall constitute a quorum, which shall be a court of record, with appellate jurisdiction, as hereinafter limited and established: *Provided, That, in a circuit where there are more than three circuit judges, the majority of the circuit judges may provide for a court of all the active and available circuit judges of the circuit to sit in banc for the hearing of particular cases, when in their opinion such action is advisable.* (The new matter proposed to be added is shown in italics.)

A subcommittee of the Senate Judiciary Committee has held hearings on the bill, but no definitive action has yet been taken in the Senate. In the House of Representatives, the Committee on the Judiciary reported the bill favorably (H. Rep. No. 1246, 77th Cong., 1st Sess), and it was passed by the House on October 21, 1941. 87 Cong. Rec. 8328 (Pamph.).¹²

¹² The report states:

"The Committee on the Judiciary, to whom was referred the bill (H. R. 3390) to amend section 117 of the Judicial

Meanwhile, in 1938, the problem was brought to the forefront in actual litigation.¹³ In *Lang's Estate v. Commissioner*, 97 F. (2d) 867 (C. C. A. 9th), the Commissioner had relied upon an earlier decision in that circuit which had been rendered by Circuit Judges Garrecht and Haney, with Circuit Judge Wilbur dissenting. The court in the *Lang* case was composed of Circuit Judges Den-

Code, as amended, with respect to the constitution of circuit courts of appeals, having considered the same, report the bill favorably to the House and recommend that it do pass.

"Under existing law provision is made that there shall be in each circuit a circuit court of appeals which shall consist of three judges, of whom two shall constitute a quorum. The bill adds a provision that in a circuit where there are more than three circuit judges, the majority of the circuit judges may provide for a court of all the active and available circuit judges of the circuit to sit in banc for the hearing of particular cases, when in their opinion such action is advisable.

"If the court can sit in banc the situation where two three-judge courts may reach conflicting conclusions is obviated. It also will obviate the situation where there are seven members of the court and as sometimes happens a decision of two judges (there having been a dissent) sets the precedent for the remaining judges. A similar result would be avoided with a court of five judges.

"It seems desirable that where the judges feel it advisable they might sit in banc for hearing particular cases. Legislation to this effect has been recommended by the judicial conference of senior circuit judges since 1938, and at its January 1941 session the conference approved the form of the present bill."

* * * * *

¹³ That same year, there was some discussion, touching upon the question, in the course of testimony by Senator Overton before a Subcommittee of the Senate Judiciary Committee on a proposal which, among other things, would increase the

man, Matthews, and Healy who disagreed with the decision in the earlier case. These judges wished neither to be controlled by the precedent established by two of the seven judges in the circuit, nor to overrule the earlier decision. But they also were of the opinion that no more than three judges might sit in the Circuit Court of Appeals, and that therefore there was no method of hearing or rehearing by a larger number. They resolved the problem by certifying the questions involved to this Court, where they were determined. *Lang v. Commissioner*, 304 U. S. 264.¹⁴

number of circuit judges in the Fifth Circuit from four to five. The impression appears to have prevailed that the circuit courts of appeals sat as three-judge courts only as a matter of practice. Senator Norris questioned "why it is not justly so, the subject of complaint that not all of the judges participate in a particular case." Senate Hearings, 75th Cong., 3d Sess., Subcommittee of the Committee on the Judiciary on S. 3233, Part 2, pp. 81-82. But the inquiry was not pressed.

¹⁴The certificate stated: "Not being satisfied with this previous decision by two of the seven Circuit Judges eligible to sit in a court in which two constitute a quorum, and three usually sit, we deem the questions here, in view of their importance, are proper ones to certify." Record in this Court, No. 919, 1937 Term, p. 5.

A situation similar to that which confronted the judges of the Ninth Circuit in the *Lang* case was presented shortly thereafter in the Fifth Circuit in *Bartels v. John Hancock Mut. Life Ins. Co.*, 100 F. (2d) 813. The result there, however, was a conflict within the same circuit upon the basis of which this Court granted certiorari. *John Hancock Ins. Co. v. Bartels*, 308 U. S. 180, 181. The possibility of the judges sitting *en banc* was not mentioned.

In 1940, the Circuit Court of Appeals for the Third Circuit, in patent disagreement with the views of the Circuit Court of Appeals for the Ninth Circuit in the *Lang* case, adopted new rules which provided for the consideration of cases, by special order, by a court composed of all the judges in active service sitting *en banc*. Rules 4 and 5 (2).¹⁵ See Appendix, *infra*, pp. 59, 60. Implicit in the adoption of these rules was the view that specific statutory amendment was not necessary. The opinion in the instant case, in which all five circuit judges concurred, sets forth both the basis for this conclusion and the administrative considerations which made adoption of the new rules desirable.¹⁶

B. THE LEGISLATIVE HISTORY

The circuit courts of appeals were established by the Act of March 3, 1891, 26 Stat. 826, which provided that there should be a circuit court of appeals in each circuit "which shall consist of three

¹⁵ The rules were adopted February 14, 1940, and became effective March 1, 1940.

¹⁶ The court reaffirmed its position in a number of other cases, at least three of which are now before this Court. *Oughton v. National Labor Relations Board*, 118 F. (2d) 486, pending on petition for certiorari No. 98, present Term; *National Labor Relations Board v. Newark Morning L. Co.*, 120 F. (2d) 262, pending on petition for certiorari, No. 307, present Term; *Southern S. S. Co. v. National Labor Relations Board*, 120 F. (2d) 505, certiorari granted, Oct. 13, 1941, No. 320, present Term.

judges." Section 2. Immediately prior to that statute the basic Federal judicial system consisted of the Supreme Court, the circuit courts, and the district courts. By creating the circuit courts of appeals in 1891, Congress brought into being a fourth set of courts, but it did not provide them with any judges of their own. Instead, it was intended that they should be held by three judges drawn from the three existing groups of judges who by Section 3 were made "competent to sit as judges of the circuit court of appeals within their respective circuits". Thus, it seems clear that under the 1891 Act it was not contemplated that a circuit court of appeals would be held by more than three judges.

In 1911, Congress enacted the Judicial Code, in which the circuit courts were abolished. 36 Stat. 1087. However, the provisions in Section 2 of the 1891 Act, providing for a circuit court of appeals in each circuit "which shall consist of three judges," were reenacted without substantial change as Section 117 of the Code. And according to the Report of the Special Joint Committee on Revision and Codification of the Laws, the section merely represented existing law.¹⁷ Section 118 provided for four circuit judges in the Second, Seventh, and Eighth Circuits, two in the

¹⁷ S. Rep. No. 388, 61st Cong., 2d Sess., Pt. I, p. 49. In the original bill this section was numbered 115.

Fourth Circuit, and three in the others. This section was intended simply to state "in concise language the number of judges now provided by law for the several judicial circuits."¹⁸ When it is also considered that this section immediately followed Section 117, it would seem that Congress must have regarded the two sections as consistent. In other words, it probably was the congressional understanding that irrespective of the number of circuit judges available for duty on the court, the court would continue to consist of three.

But apparently due to oversight, the Code did not include any provision expressly authorizing or directing the circuit judges to sit as judges of the circuit courts of appeals. Section 120 of the Code (U. S. C., Title 28, Sec. 216), in reenacting Section 3 of the 1891 Act, while retaining the provision that the Chief Justice, the circuit justices, and the district judges within each circuit, were "competent" to sit as judges of the circuit courts of appeals, omitted the circuit judges from this group.¹⁹ It may possibly have been thought that

¹⁸ Report, p. 50, *supra* note 17. The bill as originally proposed, had provided for a third circuit judge in the Fourth Circuit, but the recommendation was not adopted. Section 118 was numbered 116 in the original bill.

¹⁹ That the omission was accidental is supported by the fact that it was not noted in the report of the Joint Committee, although the report was meticulous in its description of other changes in the section. The comment on Section 118 of the bill, which became Section 120 of the Code, was as follows: "This section is but a reenactment, with slight change of language, of section 3 of the circuit court

the circuit judges became *ex officio* judges of the respective circuit courts of appeals upon the abolition of the circuit courts and that it was therefore unnecessary to describe them as "competent" to sit on their own courts. Cf. R. 54-55. At any rate, the absence of any specific provisions caused sufficient concern to occasion the adoption of the 1912 amendment, which we have described, *supra*, p. 24.²⁰

of appeals act, the changes consisting in the dropping of the word 'that' at the beginning of the section, in the substitution of the word 'shall' for 'should,' and in the omission of the words 'justice or' in the proviso, since it is not contemplated that the justices of the Supreme Court shall sit in the district courts." Report, p. 50, *supra* note 17.

²⁰ It appears from a letter written to the Editor of the Central Law Journal (74 Central L. J. 12) by Albert H. Walker, a New York attorney, that he had discovered the omission from Section 120 and had brought it to the attention of Senator Dillingham of the Senate Judiciary Committee. The letter states that Senator Dillingham's reply "was to the effect that the error had not been noticed by any member of that Committee prior to my letter calling attention thereto." Senator Dillingham suggested, however, "that if the error were to be corrected by inserting in the Judicial Code the same words that operate in Section 3 of the Judiciary Act of 1891 to make the circuit judges 'competent' to sit as judges of the Circuit Court of Appeals within their respective circuits; the Judicial Code would still stop short of making it the duty of the circuit judges to hold such Circuit Courts of Appeals." Walker thereupon drafted a proposed amendment, which he sent to Senator Dillingham for the consideration of the Judiciary Committee, and it is stated that it was the amendment, as thus drafted, which was introduced in the Senate by Senator Sutherland, and subsequently became law.

The amendment, as we have stated, provided that "the circuit judges in each circuit shall be judges of the circuit court of appeals in that circuit" and imposed upon each of them the duty "to sit as one of the judges of the circuit court of appeals in that circuit from time to time according to law." In these circumstances, it seems dubious that Congress could have intended these provisions to modify by implication the unchanged provisions in Section 117 of the Code.

2. Ordinarily a court will consist of the judges appointed to it. The statute establishing this Court,²¹ as well as the statutes creating intermediate federal courts other than the circuit courts of appeals, appear to be drafted in such a manner as to permit of no other interpretation.²² An amendment to a statute of this type providing for an additional judge would seem by necessary im-

²¹ "The Supreme Court of the United States shall consist of a Chief Justice of the United States and eight Associate Justices, any six of whom shall constitute a quorum." Judicial Code, Sec. 215 (U. S. C., Title 28, Sec. 321).

²² For example, Section 136 of the Judicial Code of 1911 provided that "The Court of Claims, established by the Act of February twenty-fourth, eighteen hundred and fifty-five, shall be continued. It shall consist of a chief justice and four judges * * *." (36 Stat. 1135; U. S. C., Title 28, Sec. 241). Section 188 of the Code provided that "There shall be a United States Court of Customs Appeals, which shall consist of a presiding judge and four associate judges * * *." (36 Stat. 1143; U. S. C., Title 28, Sec. 301).

plication to increase the size of the court.²³ The situation would be the same as if Section 117 of the Code had provided that the Circuit Court of Appeals should consist of the circuit judges within the circuit; if that were the case, it would seem that the circuit court of appeals in each circuit would consist of all the circuit judges in that circuit.

²³In 1924, the question was raised (as indicated by the testimony of Chief Justice Taft quoted in footnote 11, *supra*), whether the District of Columbia Court of Appeals could sit as a court of more than three judges, composed of the three justices of that court plus additional judges of the Court of Customs Appeals, who could be assigned to service with that court. At that time the Act provided for a "court of appeals of the District of Columbia, which shall consist of one chief justice and two associate justices * * *." Act of February 9, 1893, 27 Stat. 434, Sec. 1. Specific legislation was deemed necessary to permit the court to sit as a court of more than three judges (H. Rep. No. 58 on H. R. 4507, 68th Cong., 1st Sess. (1924)), but was not adopted at that time.

Thereafter, the Act of June 19, 1930, 46 Stat. 785, authorized the appointment of two additional justices to the Court of Appeals for the District of Columbia, and that court then sat as a five-judge court for about seven or eight years. Occasionally during that period it sat with less than five judges, and the question has been raised whether it could sit with less than its full complement. See record in *United States ex rel. Societe, etc., v. Coe*, No. 298, October Term, 1937, pp. 84-85; *Davis v. Davis*, 305 U. S. 32 (Record, p. 72, No. 16, 1938 Term).

More recently, when it was proposed temporarily to increase the number of justices of that court to six, a proviso was included "that not more than five justices of such court shall sit at any one time, to be designated by the Chief Justice." The purpose was "to assure that three justices will

But we are aware of no compelling reason why a statute cannot provide that a court, when sitting, should consist of a number of judges less than the total number appointed to it. While a court and its judges are often regarded as synonymous, conceptually they are separate entities. The classic statement is Mr. Justice Story's sitting as circuit justice, in *United States v. Clark*, 1 Gallison 497, and repeated by Mr. Justice Brewer in *Todd v. United States*, 158 U. S. 278, 284:

A court is not a judge, nor a judge a court. A judge is a public officer, who, by virtue of his office, is clothed with judicial authorities. A court is defined to be a place in which justice is judicially administered. It is the exercise of judicial power, by the proper officer or officers, at a time and place appointed by law.²⁴

constitute a majority of the court." H. Rep. No. 1057, 72d Cong., 1st Sess., on H. R. 11336. When, however, the number of justices of that court was increased to six (Act of May 31, 1938, 52 Stat. 584, Sec. 2), no comparable provision was included. Since 1938, it has usually sat as a three-judge court, although there has been some departure from that practice. In *Scripps-Howard Radio, Inc. v. Federal Communications Commission*, pending before this court on certificate, No. 508, this term, the case was originally heard by a three-judge court which decided the case 2-1 (certificate, pp. 4-49); it was thereafter set for rehearing before all six judges, and the certificate followed since they were equally divided (certificate, p. 2).

²⁴ This concept has found expression in numerous state court decisions. E. g., *Hartshorn v. Illinois Valley Ry. Co.*, 216 Ill. 392, 404; *Salinger v. Telegraph Co.*, 147 Ia. 484, 492; *State ex rel. Mayer v. Cincinnati*, 60 Ohio App. 119; *Carter's Estate*, 254 Pa. 518, 527.

This distinction would dispel the apparent inconsistency between Section 117 and the amendment to Section 118. The statute could be construed as continuing to provide for a court of three judges, drawn from a panel of such larger number whose appointment might otherwise be authorized.²⁵

3. Considered against their background, the statements in debate made by Senator Sutherland, who was in charge of the bill in the Senate, and the comment in the report of the House Committee on the Judiciary, referred to in the opinion of the court below (R. 55) are, at best, equivocal.²⁶ As suggested by subsequent remarks of Senator Sutherland,²⁷ the statements that the cir-

²⁵ Compare Article 6 of the New York Constitution which provides that the appellate divisions of the supreme court in each of the first and second departments shall consist of seven justices, and provides further (Section 2) that "No more than five justices shall sit in any case."

²⁶ Senator Sutherland stated: "It makes no change whatever in the existing law except to make it clear that the circuit judges in the various circuits of the United States shall constitute the circuit court of appeals." Cong. Record, Vol. 47, Part 3, p. 2736.

The comment of the House Committee was, as follows: "This bill deals with a defect in existing law. It makes it clear that the circuit judges shall constitute the circuit court of appeals." H. Rep. No. 199 on S. 2653, 62d Cong., 2d Sess., December 20, 1911.

²⁷ "It has been thought, as I said, that the existing law did not make it quite clear that the circuit judges shall be the constituent members of the circuit court of appeals, and it is to remove that doubt, and that only, that this bill has been reported from the Judiciary Committee." Cong. Record, Vol. 47, Part 3, p. 2736.

cuit judges "shall constitute" the circuit courts of appeals, may have been merely an elliptical way of saying that these judges shall be members of that court. That, in fact, was as much as the amendment itself specifically provided. The statements, moreover, placed their principal emphasis upon the fact that the amendment would merely cure an existing defect, and otherwise made no change in existing law. We believe, therefore, that they were not inconsistent with an understanding that under Section 117 of the Code, the court, when sitting, would continue to consist of no more than three judges.

Similarly, statements made in the debate upon the amendment in the House of Representatives do not reflect an intent to affect the existing structure and organization of the courts. Representative Clayton, the chairman of the House Judiciary Committee, who was in charge of the bill, stated its purpose as (Cong. Record, Vol. 48, Part 1, p. 667)—

specifically conferring upon the circuit judges the power and imposing upon them the duty of holding the circuit court of appeals. * * * While the provisions of sections 117, 118, 119, and 120 are in themselves probably sufficient to confer the power and impose the duty, yet, since there is a difference of opinion in the matter, it has been thought best to amend section 118 as the bill provides. It will settle any doubt

which may exist in the minds of those who believe the amendment necessary.

Representative Moon, chairman of the House Committee on the Revision of the Laws and a member of the Special Joint Committee, who had been in charge of the bill providing for the Judicial Code before the House, did not regard the amendment as necessary, but supported it as simply making "assurance doubly sure," since "it is highly important that no doubt should exist in the mind of anyone as to the competency of the judges to hold this court." Cong. Record, Vol. 48, Part 1, p. 668.²⁸

More particularly, Representative Clayton, in explaining the omission in the statute which created the problem, stated (Cong. Record, Vol. 48, Part 1, p. 667) that after the omission of the reference to the circuit judges in Section 120, "by

²⁸ In describing the situation under existing law, Representative Moon said: "The circuit court of appeals, as created by the act of March 3, 1891, is composed primarily of circuit judges. By special provisions of the act the supreme justice of the circuit is made a component part of that court, and one of the district judges may be designated to sit therein when occasion shall require it. The new act does not change these provisions. It reenacts them. It does not specifically assign the circuit judge to that court. It treats that court as composed primarily of those judges. It makes special provision for the designation of the district judge as occasion requires, and makes also provision for the precedence of the judges when the circuit justice shall attend. It treats the circuit judge as the judge upon whom the entire work of the circuit court of appeals devolves, except under the special conditions before enumerated." Cong. Record, Vol. 48, Part 1, p. 668.

some oversight the word 'circuit' before the word 'judges' was left out of section 117. Hence, it is necessary, or it is deemed by some to be necessary, to have this amendment, which, in effect, reinserts that word in section 118." However, it may be doubted that the question could have been solved merely by inserting the word "circuit" in Section 117, for this without more would have impliedly excluded from the courts the circuit justices and district judges whom Section 120 made competent to sit. But this matter of draftsmanship aside, it seems that if the amendment to Section 118 was intended to have the same effect as if Section 117 provided that the circuit courts of appeals should "consist of three circuit judges," it cannot be inferred that the amendment was intended to modify Section 117 to provide for more than three judges.

5. Finally, in the consideration of the proviso added to the 1912 amendment which made it clear that the circuit judges could still sit in the district courts,²⁹ Representative Mann, chairman of the Conference minority, who proposed the measure, referred to the fact that (Cong. Record, Vol. 48, Part 1, p. 667)—

²⁹ "Provided, That nothing in this section shall be construed to prevent any circuit judge holding district court or serving in the commerce court, or otherwise, as provided for and authorized in other sections of this Act." Act of January 13, 1912, 37 Stat. 52, 53. The reference to the Commerce Court was deleted in the Act of February 25, 1919, 40 Stat. 1156.

When the act amending the judiciary title was before the House we inserted a provision to the effect that the circuit judges might be assigned to the district court work, so that in these circuits where there were four circuit judges, one of them might be put at work in the district court.

The understanding thus implied in Representative Mann's comments, that where there were four circuit judges, the fourth judge would not sit with the others, was emphasized later in the same session, in connection with a proposal to reduce the number of circuit judges in the Seventh Circuit from four to three and to create instead an additional district judgeship. H. R. 17595, 62d Cong., 2d Sess. The report of the House Judiciary Committee, recommending adoption of the bill, stated that "Since January 1, 1912, all circuit judges became judges of the circuit court of appeals, which court consists of three judges." H. Rep. No. 240, 62d Cong., 2d sess., appearing at Cong. Record, Vol. 48, Part 2, p. 1271. Representative Evans of Illinois, in supporting the bill, observed, after referring to the fact that the circuit court of appeals is composed of three judges, that "yet we have four judges who compose that court. One of them will be idle most of the time." Cong. Record, Vol. 48, Part 2, p. 1272. And Representative Mann elaborated the thoughts that he had advanced in the consideration of the 1912 amendment, namely, that "It is to be presumed

that ordinarily where there were four circuit judges the junior circuit judge would be assigned to sit in the district court." *Ibid.* Of course, the foregoing statements are not necessarily incompatible with the conclusion that although the court ordinarily would be composed of three judges for the purpose of hearing cases, it could sit *en banc* if it so desired.

C. INFERENCES TO BE DRAWN FROM THE FACE OF THE STATUTE

Apart from the question whether the 1912 amendment to Section 118, in making all the circuit judges members of the circuit courts of appeals, was inherently inconsistent with Section 117, the various sections of the statute provide conflicting inferences as to the correct construction to be given these two sections.

1. The latter part of the 1912 amendment, making it the duty of the circuit judges to sit upon the circuit courts of appeals "from time to time according to law" may, as concluded by the court below (R. 56), merely refer to Section 126 of the Code (U. S. C., Title 28, Sec. 223), which regulates the times when the circuit courts of appeals shall sit. This appears to be a reasonable conclusion. On the other hand, it is possible to construe the phrase "according to law" to refer to Section 117 as well. If this construction were adopted, the provision would impose upon each judge the duty to sit upon the court from time to time in order to provide

the three judges which constitute the court under that section.

2. The fact that all functions pertaining to the administration of the courts are placed in the hands of the "court," is persuasive evidence that it is composed of all the judges. It is the "circuit court of appeals" which is directed to "prescribe the form and style of its seal and the form of writs and other process and procedure." Section 122 (U. S. C., Title 28, Sec. 219). "Each court" appoints a clerk, and the appointment and removal of deputy clerks, is subject to the approval of the "court." Section 125 (U. S. C., Title 28, Sec. 222). The courts are held "at such times as may be fixed by said courts." Section 126 (U. S. C., Title 28, Sec. 223). The court below pointed out that its practice was for all the circuit judges to join in the performance of such duties (R. 57). Since all the judges must perforce be interested in these matters, it would be anomalous if they did not.

Yet this point is not necessarily conclusive. The same language, even within the same statute, can have different meanings where that is required by the context and the purpose of the Act. *Am. Security Co. v. Dist. of Columbia*, 224 U. S. 491. Although the "court," upon which appellate jurisdiction is conferred by Section 117, may be limited to three judges, the "court," as that term is used in these other sections, may mean all the judges.

even though the statute does not contain specific authority for that construction.

If all the judges may properly participate in the adoption of the "rules and regulations for the conduct of the business of the court" under Section 122, there would seem to be no reason to fear the difficulties, such as those suggested by the court below (R. 57) incident to the selection of the judges who are to sit at particular sessions of the court. In the absence of any other provision as to the manner in which the selection is to be made, it may be assumed that if it is not done through informal arrangement appropriate rules might be adopted under this section.

3. Other provisions of the statute do not shed much light upon the question whether the "court" may consist of more than three judges. Thus, Section 3 of the 1891 Act, *supra*, as incorporated in Section 120 of the Code, provides that "In case the full court at any time shall not be made up by the attendance of the Chief Justice or the associate justice, and the circuit judges, one or more district judges within the circuit shall sit in the court * * *." As indicated by the court below, under the 1891 Act, it was evident that the reference in this section to a "full court" was to a court of three judges (R. 53). The only change in this section made in the Code was to change the language from "one or more district judges within

the circuit shall be competent to sit" to "one or more district judges * * * shall sit."³⁰ If the "court" is composed of all the circuit judges in active service, this section would imply that district judges could be called in whenever the court was composed of less than that number. Thus, pursuant to that interpretation, the court below could be composed, for example, of four circuit judges and a district judge. However, the court apparently does not regard its conclusion as requiring that result for its Rule 4 (Appendix, *infra*, p. 59) makes no provision for calling in district judges when it sits *en banc*.

Further complications arise if a circuit justice should sit. Under the court's Rule 4, it would seem that the circuit justice would become a sixth member of the court, rather than replace one of the five circuit judges.³¹ But if that interpreta-

³⁰ See comments in the report of the Special Joint Committee, note 17, *supra*.

³¹ Compare the situation which arose in the Court of Appeals for the District of Columbia, described in footnote 23, *supra*. Entirely moot, at the present time, would be the question of the status of the circuit judges, originally appointed to the Commerce Court, and thereafter assigned to service in a circuit court of appeals. Judicial Code, Sec. 260, 205 (see 38 Stat. 219). On the other hand, there is the question as to whether a circuit judge, who had retired from active service under Sec. 260, Judicial Code, as amended by the Act of February 25, 1919, 40 Stat. 1156, Sec. 6 (U. S. C., Title 28, Sec. 375), would be a member of the "court," if he accepted a call to perform judicial duties in that circuit. Rule 4 of the court below answers that question in the negative.

tion were to be carried to its ultimate conclusion, the "full" court referred to in Section 120 would consist of six judges, rather than five; and, under Section 120, if the Supreme Court justice did not sit, then a district court judge could be brought in to make up the full court of six. The rules of the court below do not provide for such procedure, but it would seem to be the consequence of its interpretation of the statute. The result would be novel but would not necessarily mean that the decision below is erroneous.

D. CONSIDERATIONS SUPPORTING RESULT OF COURT BELOW

Against these difficulties of technical statutory construction, based on the evidence in the legislative history and the inferences to be drawn from the face of the statute, is the fact that the opinion of the court below supports a procedure which is both inherently sound from the standpoint of wise and effective judicial administration and is consonant with the purposes underlying the present organization of the federal judicial system. The inferences are conflicting, and, in large part, the evidence in the legislative history is negative in character. The precise question now before the Court was not in issue before the Congress, and in none of the statements to which we have referred was the belief affirmatively expressed that the 1912 amendment to Section 118 of the Judicial Code did not have the effect attributed to it by the court below. Accordingly, we believe that part-

ticular weight should be attached to these fundamental considerations in the resolution of the question.

As the court below pointed out, common sense and sound practice dictate that all the judges of the court should be in a position to decide the principles of law and practice to which the court is committed. This makes for finality of decision and for the authority and prestige of the tribunal. Differences of decision deriving from the chance composition of the three-judge court will be avoided. Situations, such as those which developed in *John Hancock Ins. Co. v. Bartels*, 308 U. S. 180, and *Lang's Estate v. Commissioner*, 97 F. (2d) 867, will be resolved within the circuit.³²

³² The problem was thus posed in an editorial written in 1909 (*Federal Circuit Courts of Appeals—Their Impracticable Organization*, 69 Central L. J. 217, 219) ;

"It may be said in conclusion, that there is an essential difference between different benches of different appellate courts disagreeing with each other, and where divisions of a court differ. The court *in banc* may compose the latter differences. Where intermediate appellate courts differ, they certify this fact to the supreme court to settle.

"The prime trouble is, that each casual bench in a Circuit Court of Appeals is the court *in banc* and several of them may go on differing forever so far as any power in the court exists to prevent it. And different cases may be, and seem to have been, conclusively decided on conflicting principles in the same court."

Cf. also *McCormick's Contested Election*, 281 Pa. 281. For a general discussion of the practical aspects of the problem, see also Pound, *Organization of Courts* (1940) pp. 199-225.

These considerations acquire added significance if viewed against the background of the federal judicial system. The circuit courts of appeals are not merely intermediate appellate tribunals, but are intended to be courts of last resort in all ordinary instances. The Supreme Court's functions essentially are to "resolve conflicts among the coordinate appellate tribunals and to determine matters of national concern."³³ The procedure adopted in the Third Circuit strengthens this structure, by promoting finality of decision in the circuit courts of appeals and avoiding the necessity of further review merely to resolve conflicts among the judges within a circuit. If the procedure is not available, to that extent the structure is weakened.³⁴

³³ Frankfurter & Landis, *The Business of the Supreme Court* (1927), 255-257, 260-261, 262:

"The Supreme Court's function is for the purpose of expounding and stabilizing principles of law for the benefit of the people of the country, passing upon constitutional questions and other important questions of law for the public benefit. It is to preserve uniformity of decision among the intermediate courts of appeal." Chief Justice Taft in Hearings before the Committee on the Judiciary, House of Representatives, 67th Cong., 2d Sess., on H. R. 10479, March 30, 1922, at 2, quoted in Frankfurter & Landis, *supra*, 257, n. 10.

³⁴ Factors such as these were stressed by Mr. Justice Van Devanter, when testifying in 1928 before the House Committee on the Judiciary on the proposal to create a Tenth Circuit. He described the situation then existing in the Eighth Circuit where the court, in order to keep abreast of its work, was in practice sitting in three divisions, and stated (Hearings before the House Committee on the Judiciary on H. R.

This Court has stressed the importance to be given to such considerations in construing a statute of this character in *Am. Security Co. v. Dist. of Columbia*, *supra*. In the last analysis, we think that the conclusion here should turn upon these considerations as opposed to the competing factors which we have discussed above.

CONCLUSION

The deductions on account of the lobbying expenses were correctly disallowed. The decision of the court with respect to its power to sit *en banc* is in accord with a permissible interpretation of the statute and is supported by strong considerations of policy although the legislative

5690, 13567, and 13757, 70th Cong., 2d Sess., Serial 23, Part 2, p. 72): "It is impossible for each of those courts acting separately—although the same court—to have present knowledge of what the others are doing; and it unavoidably detracts from the continuity and harmony of their lines of decision. * * * The ~~division~~ detracts from the prestige of the court—and this notwithstanding the greatest diligence on the part of the individual judges."

And when asked subsequently whether the situation did not increase the work of the Supreme Court, he replied as follows (p. 73): "Yes; in two ways: In some cases it becomes apparent that there has not been that continuity and harmony of decisions—I am not talking about a personal want of harmony—that would be expected from a single circuit. And even where that is not apparent in particular cases, its existence in others is drawn in as a basis for seeking a review upon certiorari. Not unnaturally defeated litigants think that the other judges, if sitting, might have decided differently."

history casts doubt as to whether Congress contemplated such result.

Respectfully submitted.

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OCTOBER 1941.



APPENDIX

Revenue Act of 1928, 45 Stat. 791:

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

(a) *Expenses*.—All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, * * *

* * * *

Judicial Code:

SEC. 117. There shall be in each circuit a circuit court of appeals, which shall consist of three judges, of whom two shall constitute a quorum, which shall be a court of record, with appellate jurisdiction, as hereinafter limited and established.

* * * *

(U. S. C., Title 28, Sec. 212.)

SEC. 118 [as amended by the Act of September 14, 1922, 42 Stat. 837, Sec. 6, and the Act of March 3, 1925, 43 Stat. 1116]. There shall be in the second and seventh circuits, respectively, four circuit judges; and in the eighth circuit, six judges; and in each of the other circuits, three circuit judges, to be appointed by the President, by and with the advice and consent of the Senate. All circuit judges shall receive a salary of \$8,500.00 a year each, payable monthly. Each circuit judge shall reside within his circuit, and when appointed shall be a resident of the circuit for

which he is appointed. The circuit judges in each circuit shall be judges of the circuit court of appeals in that circuit, and it shall be the duty of each circuit judge in each circuit to sit as one of the judges of the circuit court of appeals in that circuit from time to time according to law: *Provided*, That nothing in this section shall be construed to prevent any circuit judge holding district court or otherwise, as provided by other sections of the Judicial Code.

(U. S. C., Title 28, Sec. 213.)

* * * * *

SEC. 120. The Chief Justice and the associate justices of the Supreme Court assigned to each circuit, and the several district judges within each circuit, shall be competent to sit as judges of the circuit court of appeals within their respective circuits. In case the Chief Justice or an associate justice of the Supreme Court shall attend at any session of the circuit court of appeals, he shall preside. In the absence of such Chief Justice, or associate justice, the circuit judges in attendance upon the court shall preside in the order of the seniority of their respective commissions. In case the full court at any time shall not be made up by the attendance of the Chief Justice or the associate justice, and the circuit judges, one or more district judges within the circuit shall sit in the court according to such order or provision among the district judges as either by general or particular assignments shall be designated by the court. No judge before whom a cause or question may have been tried or heard in a district court, or existing circuit court, shall sit on the trial or hearing of such cause or question in the circuit court of appeals (U. S. C., Title 28, Sec. 216).

SEC. 121. The words "circuit justice" and "justice of a circuit" shall be understood to designate the justice of the Supreme Court who is allotted to any circuit; but the word "judge", when applied generally to any circuit, shall be understood to include such justice (U. S. C., Title 28, Sec. 217).

Act of March 1, 1929, 45 Stat. 1414:

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the President be, and is hereby, authorized to appoint, by and with the advice and consent of the Senate, an additional circuit judge for the ninth judicial circuit.

SEC. 2. When a vacancy shall occur due to the death, resignation, or retirement of the present senior circuit judge of said circuit, such vacancy shall not be filled unless authorized by Congress.

* * * * *

(U. S. C., Title 28, Sec. 213a.)

Act of June 10, 1930, 46 Stat. 538:

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the President be, and he is hereby, authorized to appoint, by and with the advice and consent of the Senate, an additional circuit judge for the fifth judicial circuit.

* * * * *

(U. S. C., Title 28, Sec. 213c.)

Act of June 10, 1930, 46 Stat. 538:

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the President be, and he is hereby, authorized

to appoint, by and with the advice and consent of the Senate, an additional circuit judge for the third judicial circuit.

* * * *

(U. S. C., Title 28, Sec. 213d.)

Act of June 16, 1933, 48 Stat. 310:

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the President is authorized, by and with the advice and consent of the Senate, to appoint a circuit judge to fill the vacancy in the United States Circuit Court of Appeals for the Ninth Judicial Circuit occasioned by the death of Honorable William B. Gilbert. A vacancy occurring at any time in the office of circuit judge referred to in this section is authorized to be filled.

* * * *

(U. S. C., Title 28, Sec. 213b.)

Act of August 2, 1935, 49 Stat. 508, Sec. 1:

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the President is hereby authorized to appoint, by and with the consent of the Senate, two additional judges of the District Court of the United States for the Southern District of California, who shall possess the same powers, perform the same duties, and receive the same compensation as the present district judges of said district, and one additional judge of the Circuit Court of the United States for the Ninth Judicial Circuit, by and with the advice and consent of the Senate.

* * * *

(U. S. C., Title 28, Sec. 213e.)

Act of June 24, 1936, 49 Stat. 1903:

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the President of the United States is authorized and directed, by and with the advice and consent of the Senate, to appoint an additional circuit judge of the United States Circuit Court of Appeals for the Third Circuit, who shall possess the same powers, perform the same duties, and receive the same compensation as the present circuit judges of said circuit.

* * * * *

SEC. 3. That this Act shall take effect upon its approval by the President.

* * * * *

(U. S. C. Supp. V, Title 28, Sec. 213d-1.)

Act of April 14, 1937, 50 Stat. 64:

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the President is hereby authorized to appoint, by and with the consent of the Senate, two additional circuit judges for the ninth judicial circuit.

* * * * *

(U. S. C. Supp. V, Title 28, Sec. 213f.)

Act of May 31, 1938, 52 Stat. 584, Sec. 1:

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the President is authorized to appoint, by and with the advice and consent of the Senate, four additional circuit judges, one for each

of the following judicial circuits: Second, fifth, sixth, and seventh.

* * * * *

(U. S. C. Supp. V, Title 28, Sec. 213g.)

Act of May 24, 1940, 54 Stat. 219, Sec. 1:

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the President is authorized to appoint, by and with the advice and consent of the Senate, three additional circuit judges as follows:

(a) One for the sixth circuit;

(b) Two for the eighth circuit.

Treasury Regulations 74, promulgated under the Revenue Act of 1928:

ART. 262. *Donations by corporations.*—Corporations are not entitled to deduct from gross income contributions or gifts which individuals may deduct under section 23 (n). Donations made by a corporation for purposes connected with the operation of its business, however, when limited to charitable institutions, hospitals, or educational institutions conducted for the benefit of its employees or their dependents are a proper deduction as ordinary and necessary expenses. Donations which legitimately represent a consideration for a benefit flowing directly to the corporation as an incident of its business are allowable deductions from gross income. * * * Sums of money expended for lobbying purposes, the promotion or defeat of legislation, the exploitation of propaganda, including advertising other than trade advertising, and contributions for campaign expenses, are not deductible from gross income.

Rules of the United States Circuit Court of Appeals for the Third Circuit:

RULE 4. CONSTITUTION OF THE COURT. QUORUM.

1. *The Court—Judges Who Constitute It—Number of Judges to Sit.* The court consists of the circuit justice, when in attendance, and of the circuit judges of the circuit who are in active service. District judges and retired circuit judges of the circuit sit in the court when specially designated or assigned as provided by law. Three judges shall sit in the court to hear all matters, except those which the court by special order directs to be heard by the court en banc.

2. *Quorum—Adjournment of Court in Absence of—By Whom Adjourned.* Two judges shall constitute a quorum. If a quorum does not attend on any day appointed for holding a session of the court, any judge who does attend may adjourn the court from time to time, or, in the absence of any judge, the clerk may adjourn the court from day to day.

3: *Quorum—Interlocutory Orders in Absence of.* Any judge attending when less than a quorum is present may make all necessary interlocutory orders relating to any matter pending in the court preparatory to the hearing or decision thereof.

RULE 5. ASSIGNMENT OF JUDGES.

1. *By Whom Assigned—Disqualification of Assigned Judge—Designation of Substitute.* The three judges who are to sit in the court at each daily session shall be designated by the senior circuit judge from

time to time with the concurrence of a majority of the circuit judges who are in active service. If a judge so designated is unable to attend or is disqualified to sit in a particular matter the senior circuit judge shall designate an active circuit judge to sit in his stead, or, if no active circuit judge is qualified and able to sit, a retired circuit judge or a district judge of the circuit.

2. *Cases to be Heard by Judges so Assigned.* All matters pending in the court, except further proceedings in appeals and petitions previously heard on the merits and matters directed to be heard by the court en banc, shall be heard and decided by the judges who have thus been assigned to sit in the court at the time of hearing, if practicable.

3. *Exceptions.* Further proceedings in appeals and petitions previously heard on the merits, except petitions for rehearing, shall be heard and determined by the judges who heard the original appeal or petition, if practicable, and may be heard at any time when the court is not otherwise in session. Petitions for rehearing shall be disposed of in the manner provided by Rule 35. If a rehearing is granted the reargument shall be heard by the judges who heard the original argument, if practicable, unless it is directed to be heard by the court en banc.

SUPREME COURT OF THE UNITED STATES.

No. 34.—OCTOBER TERM, 1941.

Textile Mills Securities Corporation, Petitioner, vs. Commissioner of Internal Revenue.	} On Writ of Certiorari to the United States Circuit Court of Appeals for the Third Circuit.
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[December 3, 1941.]

Mr. Justice DOUGLAS delivered the opinion of the Court.

This case presents two problems: (1) whether a Circuit Court of Appeals may be composed of all the circuit judges of the circuit in active service, more than three in number, sitting *en banc*; (2) whether petitioner may deduct under the Revenue Act of 1928 (45 Stat. 791) certain expenses incurred by it under contracts in connection with the presentation of claims to Congress on behalf of former enemy aliens for the procurement and enactment of amendatory legislation authorizing the payment of the claims. We granted the petition for certiorari because of the public importance of the first problem and the contrariety of the views of the court below (117 F. 2d 62) and judges of the Circuit Court of Appeals for the Ninth Circuit (*Lang's Estate v. Commissioner*, 97 F. 2d 867) as respects its solution.

First: There are five circuit judges,¹ in active service,² of the Circuit Court of Appeals for the Third Circuit. All five heard and decided this case. Though they divided three to two on the deductibility of the expenses in question, they were unanimous in the conclusion that five were authorized to hear and decide the case.³

¹ Judicial Code § 118, 28 U. S. C. § 213; Act of June 10, 1930, c. 438, 46 Stat. 538, 28 U. S. C. § 213d; Act of June 24, 1936, c. 753, 49 Stat. 1903, 28 U. S. C. § 213d-1.

² As distinguished from judges retired under the provision of § 260 of the Judicial Code, 28 U. S. C. § 375.

³ The Circuit Court of Appeals for the Third Circuit has promulgated rules in accord with that view. Rule 4(1) provides: "The court consists of the circuit justice, when in attendance, and of the circuit judges of the circuit who are in active service. District judges and retired circuit judges of the circuit sit in the court when specially designated or assigned as provided by law. Three judges shall sit in the court to hear all matters, except those which the court by special order directs to be heard by the court *en banc*."

2 *Textile Mills Securities Corp'n vs. Com'r of Int. Rev.*

The problem arises because § 117 of the Judicial Code (25 U. S. C. § 212; 36 Stat. 1131) provides that "There shall be in each circuit a circuit court of appeals, which shall consist of three judges, of whom two shall constitute a quorum, which shall be a court of record, with appellate jurisdiction, as hereinafter limited and established." That provision derives from § 2 of the Act of March 3, 1891, 26 Stat. 826, which established the circuit court of appeals.⁴ Though Congress by that Act created these new courts, it did not make provision for the appointment to them of a new group of judges. It provided, however, by § 3 of that Act that the Chief Justice and Associate Justices of the Supreme Court assigned to each circuit and the circuit judges and district judges within each circuit "shall be competent to sit as judges of the circuit court of appeals within their respective circuits." Thus it is apparent that the newly created circuit court of appeals was to be composed of only three judges⁵ who were to be drawn from the three existing groups of judges—the circuit justice, the circuit judges, and the district judges.

That arrangement continued until enactment of the Judicial Code. Act of March 3, 1911, c. 231, 36 Stat. 1087. The Judicial Code abolished the existing circuit courts. § 297. It carried over into § 117 without substantial change the provision of § 2 of the Act of March 3, 1891 that there should be a circuit court of appeals in each circuit "which shall consist of three judges". Though this section was said merely to represent existing law,⁶ § 118 of the Judicial Code provided for four circuit judges in the Second, Seventh, and Eighth Circuits, two in the Fourth Circuit, and three in each of the others. An anomalous situation was presented if § 117 were to be taken at that juncture as meaning that

⁴ Sec. 2 provided in part: "That there is hereby created in each circuit a circuit court of appeals, which shall consist of three judges, of whom two shall constitute a quorum, and which shall be a court of record with appellate jurisdiction, as is hereafter limited and established."

⁵ Sec. 3 of that Act provided: "In case the full court at any time shall not be made up by the attendance of the Chief Justice or an associate justice of the Supreme Court and circuit judges, one or more district judges within the circuit shall be competent to sit in the court according to such order of provision among the district judges as either by general or particular assignment shall be designated by the court And it should be noted that after the passage of the Act of March 3, 1891, there were three circuit judges in the Second Circuit and two in each of the others. Act of April 10, 1869, c. 22, § 2, 16 Stat. 44; Act of March 3, 1887, c. 347, 24 Stat. 492; Act of March 3, 1891, c. 517, § 1, 26 Stat. 826.

⁶ S. Rep. No. 388, 61st Cong., 2d Sess., Pt. 1, p. 49, Pt. 2, p. 310.

the circuit court of appeals would continue to be composed of only three, in face of the fact that there were more than three circuit judges in some circuits. Though § 3 of the Act of March 3, 1891, made the circuit judges "competent to sit as judges of the circuit court of appeals within their respective circuits", § 120 of the Judicial Code into which the provisions of § 3 were carried eliminated the circuit judges from the groups of judges "competent to sit". Yet it retained the provision that the circuit justices and the district judges were so qualified. We agree, however, with the view of the court below that the circuit judges became *ex officio* judges of the respective circuit courts of appeal when the circuit courts were abolished. Though § 120 did not designate them as "competent to sit", its other provisions made clear that they were intended to sit. Thus, it was provided that the district judges should be drawn upon only in case the court could not be made up by the circuit justices and the circuit judges.⁷ Yet if § 117 were to be read literally, the circuit court of appeals was to "consist" of only three judges in spite of the fact that Congress had already provided in some circuits for more than three circuit judges. Clearly where there were four, all could not be members of a court of three. Yet there was plainly inferable a Congressional purpose to constitute in some circuits a circuit court of appeals of four judges.⁸

Any doubts on that score⁹ were resolved by the Act of January 13, 1912, c. 9, 37 Stat. 52, which amended § 118 of the Judicial Code by the addition of the provision that "The circuit judges in each circuit shall be judges of the circuit court of appeals in that circuit, and it shall be the duty of each circuit judge to sit as one of the judges of the circuit court of appeals in that circuit from time to time according to law." Senator Sutherland who had

⁷ "In case the Chief Justice or an associate justice of the Supreme Court shall attend at any session of the circuit court of appeals, he shall preside. In the absence of such Chief Justice, or associate justice, the circuit judges in attendance upon the court shall preside in the order of the seniority of their respective commissions. In case the full court at any time shall not be made up by the attendance of the Chief Justice or the associate justice, and the circuit judges, one or more district judges within the circuit shall sit in the court according to such order or provision among the district judges as either by general or particular assignment shall be designated by the court"

⁸ Thus the Senate Report, *supra* note 6, in speaking of § 118 (§ 116 in the bill) stated, p. 50: " . . . the section states in concise language the number of judges now provided by law for the several judicial circuits."

⁹ See the letter by Albert H. Walker in 74 Central L. J. 12.

charge of the bill in the Senate stated on the floor: "It makes no change whatever in the existing law except to make it clear that the circuit judges in the various circuits of the United States shall constitute the circuit court of appeals."¹⁰ The purpose seems plain: the size of each circuit court of appeals was not to be less than the number of circuit judges authorized by law.¹¹

And so we reach the question as to whether the avowed purpose of § 118 was defeated by § 117. We do not think it was.

That purpose was not thwarted by the provision in the 1912 amendment to § 118 that "it shall be the duty of each circuit judge in each circuit to sit as one of the judges of the circuit court of appeals in that circuit from time to time according to law." It has been suggested that "according to law" refers to § 117. In our view, however, it is the time of the sitting which is to be "according to law". Hence the reference must be to § 126 of the Judicial Code (28 U. S. C. § 223) which regulates the times when the circuit courts of appeal shall sit.

If § 117 could reasonably be construed to provide that the court, *when sitting*, should consist of three judges drawn from a panel of such larger number as might from time to time be authorized, reconciliation with § 118 would be obvious. Sec. 117, however,

¹⁰ 47 Cong. Rec., Pt. 3, p. 2736. Senator Sutherland also said: "It has been thought, as I said, that the existing law did not make it quite clear that the circuit judges shall be the constituent members of the circuit court of appeals, and it is to remove that doubt, and that only, that this bill has been reported from the Judiciary Committee." *Id.*, p. 2736. H. Rep. No. 199, 62d Cong., 2d Sess., stated, "This bill deals with a defect in existing law. It makes it clear that the circuit judges shall constitute the circuit court of appeals." And see the statements on the floor of the House by Representative Clayton, chairman of the House Judiciary Committee (48 Cong. Rec., Pt. 1, p. 667) and Representative Moon, chairman of the House Committee on the Revisions of the Laws, who had been in charge of the House bill providing for the Judicial Code. *Id.*, p. 668.

Possible inferences looking the other way are such statements by Representative Mann that "in those circuits where there were four circuit judges, one of them might be put at work in the district court." 48 Cong. Rec., Pt. 1, p. 667. And see 48 Cong. Rec., Pt. 2, p. 1272. Yet such statements are not inconsistent with the conclusion that while the ordinary complement of circuit judges would be three, all might sit.

¹¹ In this connection it should be noted that § 120 of the Judicial Code makes the "Chief Justice and the associate justices of the Supreme Court assigned to each circuit . . . competent to sit as judges of the circuit court of appeals within their respective circuits." Thus while the circuit court of appeals is composed primarily of circuit judges, the circuit justice is made a "component part" of that court. See statement by Representative Moon, *op cit.*, *supra*, note 10, p. 668.

contains no such qualification. And since it establishes the court as a "court of record, with appellate jurisdiction", it cannot readily be inferred that the provision for three judges is a limitation only on the number who may hear and decide a case. There are numerous functions of the court, as a "court of record, with appellate jurisdiction", other than hearing and deciding appeals. Under the Judicial Code these embrace prescribing the form of writs and other process and the form and style of its seal (§ 122); the making of rules and regulations (§ 122); the appointment of a clerk (§ 124) and the approval of the appointment and removal of deputy clerks (§ 125); and the fixing of the "times" when court shall be held. § 126. Furthermore, those various sections of the Judicial Code provide that each of these functions shall be performed by the "court". In that connection it should be noted that most of them derive, as does § 117, from § 2 of the Act of March 3, 1891. The first sentence of § 2 provided that the court "shall consist of three judges". The next sentence stated that "Such court shall prescribe the form and style of its seal and the form of writs and other process and procedure", etc. In that setting it is difficult to perceive how the word "court" in the second sentence was used in a different sense than in the preceding sentence. And we look in vain for any indication¹² that when those separate sentences were sectionalized in the Code, they acquired a meaning which they did not have in § 2 of the Act of March 3, 1891.

We cannot conclude, however, that the word "court" as used in those other provisions of the Judicial Code means only three judges. That would not only produce a most awkward situation; it would on *all* matters disenfranchise some circuit judges against the clear intendment of § 118. Nor can we conclude that the word "court" means only three judges when the court is sitting, but all the judges when other functions are performed. Certainly there is no specific authority for that construction. And it is difficult to reach that conclusion by inference. For to do so would be to imply that Congress prohibited some circuit judges from participation in the most important function of the "court" (the hearing and the decision of appeals), though allowing all of them

¹² Sec. 122 of the Judicial Code (§ 120 in the bill) giving the court power to prescribe the form of writs and other process and the form and style of its seal, and the power to make rules and regulations was stated in S. Rep. No. 388, *supra*, note 6, p. 51, to represent "existing law".

to perform the other functions. Such a prohibition as respects the ordinary responsibilities of a judicial office should be inferred only under compelling necessity, since a court usually will consist of all the judges appointed to it. That necessity is not present here. The ambiguity in the statute is doubtless the product of inadvertence. Though the problem of construction is beset with difficulties, the conclusion that § 117 provides merely the permissible complement of judges for a circuit court of appeals results in greater harmony in the statutory scheme¹³ than if the language of § 117 is taken too literally. And any sacrifice of literalness for common sense does no violence to the history of § 117. That history is largely negative in the sense that there is no clear statement by sponsors of this legislation that § 118 read in light of § 117 prevents the conclusion which we have reached.¹⁴

¹³ It is suggested by respondent that if the Circuit Court of Appeals may sit *en banc*, difficulties arise in connection with that provision of § 120 of the Judicial Code which reads: "In case the full court at any time shall not be made up by the attendance of the Chief Justice or the associate justice, and the circuit judges, one or more district judges within the circuit shall sit in the court according to such order or provision among the district judges as either by general or particular assignment shall be designated by the court" The difficulty suggested is that § 120 would imply that, if all the circuit judges compose the "court", then district judges should be called in whenever the court was composed of less than that number. And the argument goes further and suggests that since the circuit justice is "competent to sit" (see note 11, *supra*) then a district court judge could be brought in, when the circuit justice is absent, to make up the "full court" even though all circuit judges sat. The answer, however, is that "full court" as used in § 120 refers to the court which contains the permissible complement of judges as distinguished from a quorum of two. Under our interpretation a bench of three judges is the permissible complement under § 117.

¹⁴ Beginning in 1938 the Judicial Conference of Senior Circuit Judges recommended an amendment to the Code which would enable a majority of the circuit judges in circuits where there were more than three to provide for a court of more than three judges. Report of the Attorney General (1938) p. 23; *id.* (1939) pp. 15-16; Report of the Judicial Conference of Senior Circuit Judges (1940) p. 7. A bill was introduced during the present session of Congress in both the House (H. R. 3390) and the Senate (S. 1053) to amend § 117 of the Judicial Code by adding thereto the following: "Provided, That, in a circuit where there are more than three circuit judges, the majority of the circuit judges may provide for a court of all the active and available circuit judges of the circuit to sit in banc for the hearing of particular cases, when in their opinion such action is advisable."

This bill has passed the House. 87 Cong. Rec. 8328. In the House, the Committee on the Judiciary reported the bill favorably (H. Rep. No. 1246, 77th Cong., 1st Sess.) stating:

"Under existing law provision is made that there shall be in each circuit a circuit court of appeals which shall consist of three judges, of whom two shall constitute a quorum. The bill adds a provision that in a circuit where there are more than three circuit judges, the majority of the circuit judges may provide for a court of all the active and available circuit judges of the

Certainly the result reached makes for more effective judicial administration.¹⁵ Conflicts within a circuit will be avoided. Finality of decision in the circuit courts of appeal will be promoted. Those considerations are especially important in view of the fact that in our federal judicial system these courts are the courts of last resort in the run of ordinary cases. Such considerations are, of course, not for us to weigh in case Congress has devised a system where the judges of a court are prohibited from sitting *en banc*. But where, as here, the case on the statute is not foreclosed, they aid in tipping the scales in favor of the more practicable interpretation.

Second: The expenses in question are sought to be deducted as "ordinary and necessary expenses" within the meaning of § 23(a) of the Revenue Act of 1928. Petitioner, a Delaware corporation, was employed to represent certain German textile interests, whose properties in this country had been seized during the World War under the provisions of the Trading with the Enemy Act, 40 Stat. 411. Petitioner's employment was made with a view towards procuring legislation which would permit ultimate recovery of the properties. The estimated aggregate value of the properties was \$60,000,000. Petitioner was to be compensated on a percentage basis in case it was successful. It, however, was to bear all the costs and expenses. Petitioner launched its campaign. A publicist was retained to arrange for speeches, news items, and editorial comment. Two legal experts were retained to prepare propaganda concerning international relations, treaty

circuit to sit in banc for the hearing of particular cases, when in their opinion such action is advisable.

"If the court can sit in banc the situation where two three-judge courts may reach conflicting conclusions is obviated. It also will obviate the situation where there are seven members of the court and as sometimes happens a decision of two judges (there having been a dissent) sets the precedent for the remaining judges. A similar result would be avoided with a court of five judges.

"It seems desirable that where the judges feel it advisable they might sit in banc for hearing particular cases. Legislation to this effect has been recommended by the judicial conference of senior circuit judges since 1938, and at its January 1941 session the conference approved the form of the present bill."

But we do not deduce that this effort at clarification was or purported to be any definitive interpretation that § 117 as it stands prohibits a circuit court of appeals of more than three judges from sitting *en banc*.

¹⁵ See H. Rep. No. 1246, *supra*, note 14; 69 Central L. J. 217. And see the testimony of Chief Justice Taft and Mr. Justice Van Devanter, Hearings, Committee on the Judiciary, House of Representatives, 70th Cong., 2d Sess., Serial 23, Pt. 2, on H. R. 5690, 13567, 13757, pp. 69, 72.

rights and the policy of this nation as respects alien property in time of war. The objective of the campaign was accomplished by the passage of the Settlement of War Claims Act of 1928, 45 Stat. 254. Deductions for the amount paid to the publicist and the two lawyers were taken in 1929 and 1930, thereby producing a net loss in each of those years. Pursuant to § 117 of the 1928 Act, the net loss was carried forward two years and applied against income for 1931. The Commissioner disallowed the deductions and determined a deficiency. The Board of Tax Appeals disagreed, holding that there was no deficiency. 38 B. T. A. 623. The Circuit Court of Appeals reversed the Board.

We agree that the expenses in question were not deductible. Art. 262 of Treasury Regulations 74, promulgated under the 1928 Act was entitled "Donations by corporations" and provided:

"Corporations are not entitled to deduct from gross income contributions or gifts which individuals may deduct under section 23(n). Donations made by a corporation for purposes connected with the operation of its business, however, when limited to charitable institutions, hospitals, or educational institutions conducted for the benefit of its employees or their dependents are a proper deduction as ordinary and necessary expenses. Donations which legitimately represent a consideration for a benefit flowing directly to the corporation as an incident of its business are allowable deductions from gross income. For example, a street railway corporation may donate a sum of money to an organization intending to hold a convention in the city in which it operates, with the reasonable expectation that the holding of such convention will augment its income through a greater number of people using the cars. Sums of money expended for lobbying purposes, the promotion or defeat of legislation, the exploitation of propaganda, including advertising other than trade advertising, and contributions for campaign expenses, are not deductible from gross income."

If this is a valid and applicable regulation, the sums in question were not deductible as "ordinary and necessary expenses" under § 23(a), since they clearly run afoul of the prohibition in the last sentence of the regulation.

Plainly, the regulation was applicable. The ban against deductions of amounts spent for "lobbying" as "ordinary and necessary" expenses of a corporation derived from a Treasury Decision in 1915. T. D. 2137, 17 Treas. Dec., Int. Rev., pp. 48, 57-58. That prohibition was carried into Art. 143 of Treasury Regulations 33 (Revised, 1918) under the heading of "Expenses" in the section

on "Deductions".¹⁶ Beginning in 1921 the regulation was entitled "Donations". (Art. 562, Treasury Regulations 45.) And in the regulations here in question Art. 262 appeared under § 23(n) which covered "Charitable and other contributions" by individuals. It assumed that form and content in 1921 and appeared since then without change in all successive regulations.¹⁷ Sec. 23(n) and 23(a) both deal with deductions; and a "donation" by a corporation though not deductible under the former might be under the latter. Art. 262 purports to specify when a certain type of expenditure or donation by a corporation may or may not be deducted as an "ordinary and necessary" expense. The argument that it was not applicable because it was not specifically incorporated under 23(a) is frivolous.

Petitioner's argument that the regulation is invalid likewise lacks substance. The words "ordinary and necessary" are not so clear and unambiguous in their meaning and application as to leave no room for an interpretative regulation. The numerous cases which have come to this Court on that issue bear witness to that. *Welch v. Helvering*, 290 U. S. 111; *Deputy v. du Pont*, 308 U. S. 488, and cases cited. Nor has the administrative agency usurped the legislative function by carving out this special group of expenses and making them non-deductible. We fail to find any indication that such a course contravened any Congressional policy.¹⁸ Contracts to spread such insidious influences through legislative halls have long been condemned. *Trist v. Child*, 21 Wall. 441; *Hazeltor v. Sheckells*, 202 U. S. 71. Whether the precise arrangement here in question would violate the rule of those cases is not material. The point is that the general policy indicated by those cases need not be disregarded by the rule-making authority

¹⁶ Art. 143 provided: "Lobbying expenses.—Sums of money expended for lobbying purposes, the promotion or defeat of legislation, the exploitation of propaganda, and contributions for campaign expenses are held not to be an ordinary and necessary expense in the operation and maintenance of the business of a corporation, and are therefore not deductible from gross income in arriving at the net income upon which the income tax is computed."

¹⁷ Art. 562, Regulations 62, Revenue Act of 1921; Art. 562, Regulations 65, Revenue Act of 1924; Art. 562, Regulations 69, Revenue Act of 1926; Art. 562, Regulations 74, Revenue Act of 1928.

¹⁸ In the Revenue Act of 1926 (26 U. S. C. § 23(q), 49 Stat. 1648), Congress specifically provided for deductions of certain contributions by corporations to specified corporations, trusts, funds, or foundations, "no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation". And see the Revenue Act of 1938, 26 U. S. C. § 23(q), 52 Stat. 447.

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in its segregation of non-deductible expenses. There is no reason why, in absence of clear Congressional action to the contrary, the rule-making authority cannot employ that general policy in drawing a line between legitimate business expenses and those arising from that family of contracts to which the law has given no sanction. The exclusion of the latter from "ordinary and necessary" expenses certainly does no violence to the statutory language. The general policy being clear it is not for us to say that the line was too strictly drawn.

Affirmed.

Mr. Justice JACKSON took no part in the consideration or disposition of this case.

A true copy.

Test:

Clerk, Supreme Court, U. S.